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# Open Review of Management, Banking and Finance

«They say things are happening at the border, but nobody knows which border» (Mark Strand)

# Concluding remarks of a conference on 'Diversity and gender equality in the banks'.

by **Francesco Capriglione [i]**

**Abstract:** Both academics and practitioners have been often involved in the long-standing discussion on gender parity. This paper – which reports the conclusions of a recent conference on such topic – sought to explore the main reasons why women remain under-represented in senior and middle management positions within the financial sector. Building on the idea that gender diversity may improve key performance indicators, the study focuses primarily on the argument that – even though several barriers are still restricting women's access to managerial roles – stereotypes and other bias must be overcome in order to enhance female contribution to the overall success of the business. However, as highlighted in the analysis, career progression needs to follow the basic principles of meritocracy since individuals must be evaluated according to their skills and competences – and so independently of their own gender.

**Summary**: 1. Introduction. – 2. The issue of gender parity. – Diversity and banking governance: the perspective of a review of business models. – 4. European guidelines on the active role of women in management. – 5. The need for equal opportunities in spite of gender diversity.

1. Wanting to begin these brief remarks with personal memories, distant in time but yet interesting with regard to the subject of today's meeting, the thoughts turn back to my first job started more than half a century ago, in the Bank of Italy, institution in which, at the time, women were not allowed into the managerial career, but only in the administrative one . Significant, also, was the fact that the female staff – according to the strict internal rules – was required to wear an dark apron , almost having to hide their appearance, in a logic of homogenization to standardize the female members, and clearly stress out their gender diversity.

There is no doubt – as nowadays reports show – that fortunately such a blatant female subordination (seen in the past even in the largest Italian financial institution), now survives only in the memories of those who, when young, , lived in a socio-economic context that is hopefully now definitely disappeared.

First, I'd like to highlight that the thesis supported today are far from easy rhetoric, which usually characterizes the remarks on issues related to the rights claimed by the women's movement; thesis that are also affirmed to overcome unjust discrimination related to diversity (religious or racial one, but also homophily, etc.). Indeed, the debate today wants to rely upon balanced and logical arguments (both technical and legal) in order to explore and clarify the issue under observation.

2. In particular, the debate focused on the topic of "*diversity*" in the EU framework, underlining how difficult the path towards satisfactory levels of "*gender equality*" has been in the recent years. It seemed significant, on this issue, the report regarding the increase (above the 20%) of the so called "*female quotas*" in the boards of directors of Italian firms (Parrella).

At the same time, it's worthy to consider also the convenience of whether delegating the identification of "*gender equality*" to the lawmaker's intervention; this tendency, ascertainable in the Italian legislation (see Law n. 120 of the 12th July 2011), while not appreciated by some countries, such as the United Kingdom, has been an incentive for others, such as Germany, to promote some legislative amendments in this field (Brogi, Perrazzelli, Sciarrone).

From previous observations and hypothesis, it has clearly emerged that "*gender diversity*" – and, therefore, the maintenance of unequal distinctions in the access to certain professional "careers" (as well as in the prospects for career progression- is a display of an *ideological conservatism* not annihilated yet, despite the relevant legislative amendments therein adopted, in compliance with the high levels of "juridical development" recently achieved. The solution of this problem has to be found by taking into consideration the specific cultural level of those countries engaged in its definition; hence the opinion according to which in countries like Italy it has to be deemed as opportune (if not necessary) the lawmaker's intervention in order to overcome a long-standing paralysis, that otherwise could have lasted even longer (Perrazzelli).

I do not want to focus any further on these debate's topics; nevertheless, I intend not to conceal an idea that seems to stem from today's reflections: I am referring, particularly, to the fact that a more complete (and hopefully ultimate) acknowledgment of "*gender equality*" is going to take a long time. This consideration is confirmed by the unequivocal observations made by some scholars (especially: Brogi and Zucchetti), as well as by the update, given to the audience, that among ABI's "Executive Committee" there are no women (Zaccaria).

That said, it is obvious that it will be necessary to proceed in the direction of improvement, as it seems to be emerged from the suggestions expressed in today's speeches. Defeating the blind logic at the basis of the situations here criticized since now is, therefore, the aim to pursue, knowing that its fulfillment is strictly connected with the solution of the more general problem of searching for an enhancement of the "quality of life" among Member States (Perrazzelli). Moreover, it is necessary to specify that this path is an uphill struggle, that has to be undertaken by being convinced that a a vast part of the civil society must not be exposed to the deprivation of freedoms and rights granted on a constitutional level to all the citizens equally (Pellegrini, Zaccaria).

3. In engaging the topic under consideration, most of the rapporteurs focused on evaluations regarding the difficult and recent financial crisis that, as is known, affected numerous countries of the Western area, causing a recessive phase and economic stagnation that only now seems to

come to an end It has been stressed, thereof, that in order to start a real reinforcement of the economic recovery, an action from the credit industry, especially responsible and professionally qualified, is needed.

Hence the necessity to search for a *management* composed of people with considerable technical ability and remarkable cultural sensitivity; a search that becomes the prerequisite of an *agree* which aims to guarantee the adequate and efficient functionality of the business organizational mechanisms (to which it is delegated the opportunity of improving the credit sector, making it more transparent and efficient than how it appears nowadays). It is become definitive, therefore, a context that requires, in order to achieve an effective management balance, administrative and supervisory bodies among which the gender differentiation could generate useful effects, improving the quality of the internal debate and posing on innovative basis the dialectical discussion between the business's members.

Upon this theoretical prerequisite accurate considerations have been engaged, in order to correlate *diversity* to the definition of a banking governance, which is functional to a closer cooperation between industry and finance (Bianco, Pellegrini, Ramasco, Sciarrone); thus, highlighting some of the most significant issues raised, at the European level, to identify adequate rules for optimizing managements.

This part of the debate, regarding the possibility of achieving higher forms of economic development through *diversity,* brings back the renowned thesis of Daniela Del Boca, according to which "women's work makes economy grow"; assumption that was used years ago for underlying the importance of female employment, with the intent of encouraging its appreciation. In conclusion, the observations expressed by today's speakers indicate that the aforementioned statement does not limit its impact with conveying – based upon an accurate economic analysis – a "*favor*" towards female participation in the labor market; the useful effects that can be deduced from this participation go far beyond a significant increase in the growth process, which is a conceivable result especially in those countries characterized by gender gaps in employment rates.

Right now, we are entitled to formulate an interpretation of the idea of women as participating to the productive model that allows us to attribute to the aforementioned formula the relevance of a "guideline", in order to reconsider the benchmark of business organizational structure. This formula, indeed, seeks for a new definition of business, different from the one that, until a recent past, characterized its essence. This is a first conclusion that can be deduced from this conference! It presents a specific topicality in the banking field, in which the principle of *gender equality* has been fairly recognized only recently; this, with the obvious negative consequence of having deprived, for a long period, the financial activity of the significant contribution that could result from women's presence in decision making and top management roles.

4. Then, the speakers (Bianco, Falci, Guglielmetti, Pellegrini) have quoted some EU directives (e.g.: 2013/36/EU dealing with credit and investment companies; and, more, Regulation 575/2013/EU – the so-called CRD IV/CRR; as well as the directive 2014/65/EU about financial instruments' markets – the so-called MIFID 2). It is literally inferred the orientation of the European lawmaker to give importance – above all in the regulation of corporate governance field – to the variety of 'capabilities' and 'points of view' of the members in the *administrative* and *audit boards*. Therefore, it outlines an evaluation parameter acknowledging an active managing role of women, in keeping with their professional capabilities and work experience.

An acknowledgement comes from the European lawmaker, whose aim is to involve those willing to seek for building a 'common house', where the woman will, at last, have a central role, gained through an evolutionary process where a sort of cultural revolution, started more than a century ago, has been fulfilled. This is more significant in finance rather than in other fields; actually, in this field women have long been victims of a prejudice which has not allowed them to run for positions suitable to their intellect, to the peculiarity of their temper which makes them particularly fit to make decisions where rationality goes along with intuition in assessing risks.

Since the end of the $19^{th}$ century up to now the Nora of Ibsen's 'A Doll's House' has gone through a way full of obstacles to reach her goal, not yet complete achieved in my opinion, although the woman's path – as it is coming out from the conclusions of this meeting (Amorosino, Siclari) – is acquiring a new perspective. Hope is being replaced by the certainty of achieving a goal, remarkably significant from an ethical profile as well, since the principle of equality among genders gains particular value if its grounds are ascribed to the aim of enriching society. The latter will, then, have the chance to benefit from an innovative cultural and practical input, featured by knowledge and techniques, which are not – or better, not willing to be – in contrast to the ones normally referred to man; rather, they aim at integrating their contents and improving their quality towards greater expectations to reach useful results for everybody (Bianco, Brogi, Pellegrini, Perrazzelli, Ramasco, Sciarrone).

The guidelines given in this meeting suggest that the path of woman's social and cultural emancipation (implied in achieving freedom from an age-old psychic and behavioural subjection to man) is going beyond the mere encouragement of female employment policies. It is no accident that a trend concerning gender equity issues converges on common interests. It is, then, clear that a school of thought limiting and compressing women' true and expanding power at work means refusing progress; indeed, it allows to identify a persistent deplorable custom of mental violence damaging those who have been abused by a selfish, surely blameworthy, domineering will. On the other hand, every action clearly addressed to disregard gender equality ends up with an outdated attempt to force the historical process.

The views here shown, which reaffirm the needs for enhancing women's role state the widespread belief that their progressively growing presence on the 'job market' is able to activate a virtuous circle ending up with advantages for the whole economic system. In particular, referring to finance, the empowerment of women's active role is likely to promote management practices shaped on higher levels of prudence, consequent to a peculiar care from those who, thanks to their moral integrity, avoid risky behaviour and pay special attention to complex circumstances.

5. Before closing these brief thoughts I would like to present you with some of the questions that I asked myself before participating to this seminar.

I am mainly referring to the identification of the reason why – especially in certain countries and in contexts characterized by delays in the economic development– women had to suffer a sort of penalization, becoming subject to the representatives of the male sex. The answer to this question must be found in the weak position in which women found themselves , starting with the biblical link to Adam's rib. Certainly, their peculiar physiological connotations and the fact that women are destined to be mother and wife have eased the idea of their weakness in comparison to the power of men, intended in its broader sense (Brogi, Zaccaria); this convincement has contributed to woman's social placement (as previously expressed), negatively influenced also by the necessary balancing between family and work commitments (to which she was forced).

A deeper evaluation of the problem in question highlights that the specific *status* of women – and, therefore the unequal regime that they suffered through time because of the difference in gender – is essentially linked to cultural factors. It is not just a coincidence that women's statuses appear to be less important (in comparison to men's) mainly in undeveloped countries or ones dominated by religious ideas that are not afraid to accept logics in which women are configured as instrumental to the needs and desires of the exponents of the opposite sex, nearly in order to justify the influences that mortify their social role.

Another question, to which I have not been able to answer, concerns the influence played by the *technological progress* on the market's legal order. This progress highlights a new reality in which – as clarified by Giorgio Oppo a few years ago – a «depersonalization of relationships» reduces the historical identity of the individual. This dehumanization process – which mainly influenced the contractual term sand the delicate sector of financial operations – involves also the organizational profiles of businesses, since technology inevitably entails a *simplification* of the decisional schemes, a reduction of the *responsibility* in the presence of functions (such as *risk management, internal audit and compliance)* preordained for risk evaluating and containing risks and, therefore, limiting the riskiness of the financial intermediation.

In the light of this, in reference to an increasing orientation towards the acceptance of the operational forms that come to business results often not entirely shared, the question is: which implications (also prospectively) may arise from the future distribution of tasks between men and women? Will we also find the affirmation of a «physicality» connected to technology that, according to Natalino Irti, limits intersubjective encounters and reduces dialogue, consequently slowing down the development towards gender equality, of which we have deeply talked about today? Or is it that thanks to the increased ability of women to adapt to change, because of their natural sensibility that induces them to be wary of automatisms (and, therefore, to pay special attention to the verification of the results that affect strategic choices) they will deliver a better performance as compared to that of their male counterparts?

These are difficult questions to answer. . A solution to them may come from the adoption of measures aiming at rebalancing the subjective positions, organized consistently with the changes presented today.

Therefore, I would like to conclude by recommending special attention for *false problems*! And with that I do not want to label as 'false' the problem of «gender equality», but I would like to highlight that an excessive insistence (at times inadequate) on the need to find solutions to this topic is likely to make us forget that this equality cannot exclude the comparison between the skills of persons of different gender. Therefore, the equality that must be sought is that of «similar conditions» required for a job and for the progression in its performance; thus it seems that a correct intervention would be the one that instead of continuing to affirm the need for a homogenization between men and women reaffirms the need to ensure equal opportunities for all, despite "gender diversity".

[i] Concluding speech of the Conference on «Diversity *e parità di genere nelle banche: dalla* soft law *all'attuazione della* CRD IV», University Sapienza, Rome, 17 april 2015

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«They say things are happening at the border, but nobody knows which border» (Mark Strand)

# Gender Diversity and Financial Intermediaries


by **Mirella Pellegrini**



**Abstract**: The paper analyzes some recent rules (Directive 2013/36/EU, called CRD IV and Directive 2014/65/EU, called MIFID 2) oriented towards a modern financial management focused on people with great expertise and managing abilities, but at the same time diversified by age, sex, geographic provenience and experience. The goal is to identify ways to produce a strategic plan filled of the most different contributions to provide innovative solutions. The introduction of more diversified administrative organs is intended to contrast the "group mentality phenomenon", through the representation of "a variety of points of view and experiences". This research highlights the fact that women move in an under-confidence context (unlike men, who are usually overconfident) that often causes them to accept decisions even when not fully in agreement. Moving on to the identification of the reasons that justify a more appropriate placement of women in the banking and finance enterprises, the Author emphasizes the need for a particular technical qualification of the activity performed by the board of administration and control of the institutions belonging to this sector. Indeed, the various options (from organization to investment) for decisions oriented towards sound and prudent management require the ability to assess a balanced evaluation of information data remitted to the boards of directors and control in the reports that the structure periodically prepares.




1. I'm delighted to participate to this convention on women and their (important) role in the financial world.*

This conference reflects a great transformation that's taking place in many countries (including ours) and that wants to give an insight on the actions taken by the European and National regulator to safeguard the existence of more efficient corporate governance mechanisms.

In fact *governance* is the topic of our discussion, since the quality of the decisions taken has a fundamental impact on the efficiency of the organizational bodies (*rectius:* of banking) and, consequently, on the performance of our financial market (that today more than yesterday needs competition, seriousness and the ability to find innovative solutions to the actual and more and more social and participative context).

The financial crisis, the economic recession and the new legal criteria, have highlighted the difficulty in supporting the economy and, therefore, the Italian recovery. In light of the overcoming of these difficulties, Italian companies, especially bigger sized ones, highlight a regulative solution orientated towards a management made of people with great expertise and managing abilities, but at the same time diversified and complementary by age, sex, geographic provenience and experience, in such a way as to produce an opinion filled of the most different contributions and confrontations (as such, more open to innovative solutions). Hence the need to avoid in every possible way that within these there is a poor dialogue and confrontation, in order to ensure the correct and efficient functionality of the government bodies.

This is possibly the way to stimulate a *virtuous* development of the economic *agere* in line with the affirmation of an entrepreneurial type characterized by a greater transparency and attention for the (correct) risk management than before today, such as to organize the management accordingly to the decisional balance criteria.

In this introduction, I would like to start my observation from the considerations contained in some Directives previously mentioned by those who intervened before me (I am referring to Directive no. 2013/36/EU on credit and investment institutions; to Regulation 575/2013/EU so called CRD IV/CRR, and to Directive 2014/65/EU, on financial markets, so called MIFID 2).[1] These highlight the importance of "different abilities and points of view, and also the correct professional experiences", already stressed in the Green Book of the European Commission on corporate governance (2011); they confirm that "a greater difference fuels the debate, promotes alertness and the questioning of certain decision with the board of directors and, potentially, improves the quality of decisions."

The introduction of more diversified administrative organs is intended to contrast the "group mentality phenomenon", through the representation of "a variety of points of view and experiences"; in other words it has the objective of "improving risk oversight and the resilience of institutions", that is, their ability to cope with traumatic events and to reorganize their *agere* in a positive way (recital 60, Directive 2013/36/EU).

This is a significant guiding principle, reaffirmed in the transposing by the Bank of Italy of the European governance regulation[2], well known to scholars and professionals (including myself, I have often recalled this regulation in my past works) from which we should not deviate in the design of efficient firms and markets characterized by a high level of liquidity, transparency and proper operation; this criteria was intended to represent the best guarantee for investors that access the capital market, becoming essential for its proper functioning.

2. From what has already been said, I believe that it is not necessary for me to dwell and focus on the fact that gender parity answers primarily to the need to satisfy the principles of fundamental fairness between citizens, as stated in the Italian Constitution, in particular in articles 3 and 51.

Nor do I intend to reiterate the EU guidelines on gender balance in the government bodies of enterprises. On this topic one should also pay attention to the Directive Proposal (which I recall to be stranded) aiming at ensuring equality and equal conditions between men and women, while leaving the Member States free to determine the ways and rules to achieve this policy target.

I also will not dwell on the assessment of the productivity levels that characterize the corporate structures in which there are some women (mentioned earlier by other colleagues); limiting myself to reiterate that gender inequality negatively affects management performance since in such structures, if there is a significantly low number of women, very little access solutions oriented towards equality logics, to be considered as necessary to optimize the redistribution forms.

This assumption is confirmed, moreover, by a recent study carried out by the Max Planck Institute in Jena by a group of experimentalists *of (the University where I come from)* the LUISS Guido Carli University in Rome (Laboratory of Experimental Economics "Cesare") that tested the hypothesis that women are more "suspicious" than men, while negotiating. This hypothesis is based on the evidence that people who belong to groups that have been historically discriminated, such as ethnical minorities and women, have less trust in their counterparties and consequently behave in a more strategic way[3]. This would be the reason why women have become more adverse to risk, but with greater ability to verify the reliability of others and to adopt strategic behaviors[4].

This research has, however, highlighted the fact that women move in an under-confidence context (unlike men, who are usually overconfident) that often causes them to accept decisions even when not fully in agreement.[5] In general, lab experiments, carried out in different countries and with different samples, have all highlighted some recurring characteristics: women are in average more adverse to risk, less self-confident and more willing to accept non-promotional tasks and lower earnings than men[6].

At the same time, it was found that – despite an under-confidence attitude on paper – women are more prone to change and learn to adopt "dominant" behaviors very quickly, being able to apply them with great success; there where, situations that express the result of appropriate training and integration/collaboration (e.g. when women "team up" with each other) show better results, such as to exceed the limit of an *agere* influenced by fear and by the suspicion of women who realize the weight of their belonging to a minority.

These characteristics tend to fade with experience and should often be attributed to influences and social and cultural gaps rather than genetic heterogeneity.

On this topic, the Generali Investments Europe Case should be analyzed: in2015 this company has decided to devote resources to enhance gender diversity, considered as a strategic project. Therefore, it has chosen to support female representation within the company[7], while deciding to actively participate to the promote women's professional growth[8]. This with the specific intent to build an inclusive model that supports the expression of all talents focusing on meritocracy: teamwork and the enhancement of diversity for the multiplication of quality, richness of ideas and solutions.

I will avoid any consideration on the predictable, desirable end of the phenomenon in which we are concerned, whose value in a limited period of time seems to be deduced from the remarkable numerical expansion of the presence of the female gender in university studies and, what is more important, their better performance in terms of preparation and results.

Instead, I would like to spend a few words to analyze and understand if the principle we are dealing with applies mainly to the financial and banking sector, field in which traditionally only marginal parts are left to women, preventing them from giving a constructive contribution to an activity that can take advantage of women's intellectual and cultural specific characteristics.

Therefore, the logical procedure to test the validity of the presence of women in banking and financial contexts must start from the consideration that the whole regulation of this sector involves the general principles of civil society in order to improve the explanatory modalities. Firstly, the protection of savings (art.47 Cost.) and, therefore, the submission to public scrutiny of the subjects who exercise banking and finance are considered as priority moments of a larger legal complex that has targeted the dignity, assessed in its man/woman unitary configuration, that is without discrimination[9].

Dignity, fairness, equality are social principals that are part of the banking system since the 1930s and that are offered to the clients, to those who benefit from the services offered, savers … Naturally time goes by also affecting the interpretation rules for the values underlying a systematic construction of the financial reality. These principles are about to be brought within the organization, and gender equality and diversity become a garrison to ensure the sound and prudent management, almost equal to those already known, such as the Chinese walls on conflicts of interest , transparency, operative fairness.

It is clear that if gender equality is an intrinsic detail of the essence of banking activity, it does not seem feasible in any way to admit differentiated roles with regard to the identification of organizational models through which that activity is exercised.

This is the premise on which the debate on the legitimacy – or more precisely the justification – of the recognition of a more suitable location within the sector for women, should be based[10]; the crystallization of the organizational models focused on the admission of assumptions different from those analyzed is not acceptable.

3. Moving on to the identification of the reasons that justify a more appropriate placement of women in the banking and finance enterprises one should highlight the need for a particular technical qualification of the activity performed by the board of administration and control of the institutions belonging to this sector. Indeed, the various options (from organization to investment) for decisions oriented towards sound and prudent management require the ability to assess a balanced evaluation of information data remitted to the boards of directors and control in the reports that the structure periodically prepares.

Therefore, this is an activity characterized by an intuition not detached from the reference to the analytical data that characterizes the different circumstances under observation; all requirements which, in the collective, are considered typical of women as they are easily correlated to the psycho-physical qualities that characterize their personality[11]; to these requirements it is appropriate to add a careful and punctual way of viewing the reality under observation (but also able to move in different directions), as it is necessary to understand the complexity and, thus, to prevent any degenerative effects of the process examined by the border.

It goes without saying that an accomplished performance of that business requires dedication and commitment, and could prove itself to be difficult to combine with women's traditional role in society.

In terms of concreteness, this is an intrinsic spare factor and explains why sometimes "businesswomen" are victims of family isolation and, in most cases – especially in our country – can play primary roles only in old age.

That said, it seems appropriate to highlight that, in the latest knowledge techniques, the contribution of women, within the financial market (based primarily on tests that assess psychological correctness), in identifying appropriate remedies to market asymmetries is significant[12]; contribution that women are able to carry out thanks to their specific ability to relate to others, to their sensitivity in taking into account other people's demands.

In fewer words, the intuition – or more precisely women's natural ability to contrast men's deductive rationality with a decision-making guideline particularly sensitive to perceive the orientation of others – causes gender parity (and/or diversification) to become instrumental to the achievement of more profitable management, which thanks to women may benefit from their inclination towards mediation in conflict situations and from their natural limitation of risks, which is known as typical trait of the female personality (as shown by scientific analysis) [13]. This without giving up on listening to other people's advice, accepting innovative criteria for the *agere* evaluated in the entirety of their essence and, therefore, with special care to avoid that the same can be attributed to mere power logics (women are naturally ready for multitasking, they tend to be more cooperative in addressing problem solving situations and are motivators for working groups). In particular, gender parity is ideal to introduce suitable forms of balance within the management. These forms should be related to the peculiar independence of corporate officers and, therefore, related to the independence of the choices of the board from any interference arising from the lack of autonomy of its members[14].

In my opinion, this is the context in which we should place the interpretation of the interlocking and multiple directorships prohibition recently introduced in the banking and financial sector (art. 36 l.d. 201/2011, so called the "Salva Italia" decree)[15], in order to reaffirm – in different ways and on different levels, in reference to the CRD IV – the need of the non-existence of constraints or limitations in the identification of members of the administrative and control borders; both, in my opinion and obviously, are meant to encourage the plurality of approaches and perspectives in analyzing problems and in taking decisions, as well as rewarding professionalism, through a balanced composition of the bodies (avoiding the risk of behaviors of mere alignment to prevailing positions, internal or external to the bank).

The interlocking prohibition, seeks to prevent connections between competitors of the banking, financial and insurance market, organized through the presence of the same corporate officers. A healthy competitive market should avoid the crystallization of the list of those who may have management responsibility.

Instead, the CRD IV, for "internal" reasons aiming at the sound and prudent management of large banks, through diversification aims at ensuring  time devotion (further guiding principle of the new rules of governance).

Therefore, we are in the presence of a *voluntas legis* aiming at affirming a meritocratic logic: avoiding the proliferation of charges in a few subjects ends up expanding the number of potential recipients of the boards and – at the same time – introducing a limit to the hoarding of these roles by persons who may be linked in various ways to the production centers or to empowering roles. Hence the expected benefit resulting from the policy of gender equality/diversity in redefining the composition of the board of directors in accordance with the parameters laid down by that regulation[16].

4. One last thought *in subiecta materia* can be drawn from the information provided by the recent financial crisis, which has shown the need to improve the efficiency of the organizational structures which reflect the optimality of financial services.

At the same time, the need to introduce balancing elements to management has appeared:  on the one hand avoiding moral hazard behaviors, on the other suggesting the opportunity to re-analyze the matter of corporate officers' compensation.

The presence of women in boards of directors and audit committees will develop good behavior (and, therefore, a more transparent and balanced action of financial firms) and will allow potential savings on costs related to the reconfiguration of the wage system (thanks to the expansion of the number of recipients for the positions). For real, it is likely to witness a general inclination of women to the acceptance of lower wages since taking leadership roles for them is rewarding in terms of personal satisfaction, considering a generational release for this reason allowed to the female gender.

If this can happen at first, it does not have to represent the effects of a change, because a choice oriented towards reduced salaries that would create a new gender gap would be unacceptable ("Choose us because we cost less"). The result must and can only be "choose us women because we are very respectable".

Therefore a reflection in terms of equal pay as well as of representation in boards is necessary.

5. I'll conclude my thoughts with a further clarification on the distinction between the principle of gender parity and the broader concept of gender diversity. The first one (inferable from important European Documents, such as " Strategy for equality between men and women", and the "European Pact for Gender Parity"), has found expression in the Directive proposal on administrators without executive roles in listed companies; according to it by 2020, 40% of these will have to be exponents of the underrepresented sex, to which priority should be given over the candidates of the opposite sex, with the same qualifications.

The second one – on the diversification criteria within management bodies, according to "age, sex, geographical origin and educational and professional career" – is set out, as stated in Directive 2013/36/EU on credit institutions and investment enterprises (so called. CRD IV), and in Directive 2014/65/EU on financial markets (so called. MIFID 2).

In fewer words, while gender parity is achieved through an automatic mechanism connected to predefined percentages, the evaluation of diversity, including the gender issue here, requires transparent comparative evaluation of heterogeneous profiles, performed accordingly to company-specific needs. Such balancing, as a talent management practice aims at improving business efficiency, obviously invests equally in men and women and must be a gender parity objective.

More recently, Directive 2014/95 / EU on non-financial information and diversity in the composition of the governing bodies[17], went further, revealing the existence of a functional link between diversity and disclosure: the introduction for more adequate transparency in the management of the issue in question should encourage companies to consider the problem in question more carefully, directing them towards greater attention to the need to ensure higher levels of diversity in their boards[18]. This suggests that the establishment of a transparent system is needed not only to inform the market (about the corporate governance practices) but also to "create indirect pressure on companies to push them to diversify the composition of their board" (Directive 2014/95/EU)[19].

Hence the importance given to the so called saving clause, according to which large listed companies will have to disclose the management criteria adopted on diversity (extended to include the objectives, implementation methods and achievements), or their reasons for not doing so[20].

It is clear that this is a new impulse to accept the importance of diversification; for this reason, we come to a disciplinary system that allows (through the clarification and disclosure of the management rules) to achieve a systematic order increasingly characterized by the affirmation of real gender parity.

In the outlined context, we should also consider the provision contained in the Vigilance Regulation of the Bank of Italy (Circular 285/2013 as updated in the implementation of CRD IV) [21] of a link between diversification policies and transparency requirements. Considering carefully, this provision was already contained in the Recommendations of the Code of Conduct drawn up by the Committee on Corporate Governance for the Italian Stock Exchange; it is clear how sometimes self-regulation is able to anticipate the best solutions for the company's good performance. I feel obliged, however, to express my personal mistrust in a rejection of well-established professional statuses, managerial roles, remuneration and other satisfactions, left to the voluntary initiative of the market and its agents; this, especially when it comes to the financial market where us women, even if invited to participate in decision-making and management bodies of the industry, are sometimes forced to adapt to consolidated male logics.

Therefore, the regulative imposition (I'm referring to EU directives and national legislation, already in force with Law no. 120/2011) of diversification implemented through binding measures with regard to women's representation is well appreciated; unlike that which is given to deduce from the approach adopted by the international IOSCO, which calls for the initiative of a voluntary change (a cultural revolution) that should prove itself as historical[22]. This is the orientation that I propose here considering it fully justified by the fact that Member States have not shown so far any significant progress when left to their autonomous choice. Likewise I feel it is appropriate to fully agree on the temporary nature of the measures introduced, meeting the desires of those who – like me – believe in meritocratic system.

The important thing is not to fall in the misapplication of the rules, as was rightly highlighted a few years ago in the newspaper "l'Avvenire" stating "the false value of non-discrimination prevents thinking, evaluating, discerning and expressing, as well as that of transparency that is often alien to the search for truth."

This is a modern version of what has already been supported by Tomasi di Lampedusa nearly sixty years ago, when he wrote: if we want everything to stay the same, it is necessary for everything to change. Let's try and prevent it..

*** Report of the Conference "Diversity e parità di genere nelle banche: dalla soft law all'attuazione della CRD IV", Rome, La Sapienza University, 17th April 2015**

[1] The Directive 2013/36/EU, also implemented in Italy, in defining the new EU regime on capital requirements of the banking system, has asked the Member States and competent authorities to require institutions and their nomination committees to stick to a wide range of quality and expertise in selecting the members of the management body and to prepare for that purpose a policy that promotes diversity within it.

The competent authorities are therefore obliged to provide this information to the EBA, which will compare the records concerning Diversity within the Union in order to adopt, within the 31st of December 2015 orientations on "the concept of diversity to be taken into account for the selection of the members of the management body".

[2] See. Circular n. 285/2013 Bank of Italy, VI update of the 6th May 2014, section. Titolo IV, chapter 1 "Corporate Governance".

[3] See ALESINA and LA FERRARA, *Who trusts others?* , in *Journal of Public Economics*, vol.85, 2002, p.207 ff.

[4] See DI CAGNO, GALLIERA, GUETH, PACE e PANACCIONE, *Make-Up and Suspicion in bargaining with cheap talk. An experiment controlling for gender and gender constellation*, in *Theory and Decision*, currently printing, 2015.

[5] There is a extensive experimental evidence of gender differences both in the choices taken in risk condition and uncertainty (see ECKEL and GROSSMAN, *Men, Women and Risk Aversion: Experimental Evidence*, 2008, in *Handbook of experimental economics results*, Vol. 1, Ch.113, 2008, p. 1061 ff.) and in the bargaining (AYRES and SIEGEKMAN, *Race and Gender Discrimination in Bargaining for a New Car*, in *The American Economic Review*, Vol. 85, n.3, June 1995, p. 304 ff.; NIEDERLE e VESTERLUNG, *Do women shy away from competition? Do men compete too much?*, in *The Quarterly Journal of Economics*, August 2007, p. 1067 ff.

[6] See GNEEZY e RUSTICHINI, *Gender and Competition at a Young Age,* in *American Economic Review*, 2004, p. 377 ff..

[7] Here is some values on the female presence in the group: 15% of the first levels are women (3/20). On secondary levels women represent 35% of the total (29/84). Overall, the presence of women in the company is equal to 33% of the workforce (129/390). There are also 2 women in the Board of Directors.

[8] This is achieved through various initiatives: female empowerment training, with two targets: young women and those in career development; gender communication training; company meetings with role models, i.e. models to inspire; rethinking certain human resources processes (such as recruitment) aiming at encouraging a mix in genre, where possible. In this commitment the priority is to combine gender equality and meritocracy (to make sure that it does not become the first and only priority)

[9] See. Circular no. 285 Bank of Italy, amended May 6th 2014, Titolo IV – Chapter 1, Sec. 1, according to which " The corporate governance of banks, in addition to responding to the interests of the company, must ensure sound and prudent management conditions, the essential regulatory objectives and supervisory controls."

Furthermore, in Sec. IV: In qualitative terms, the proper performance of the functions mentioned requires the following subjects in the organs with strategic supervision and management functions: with widespread skills between all the components and appropriately diversified, so as to enable that each of the components, part of the committees and of the collective decisions, can contribute, among other things, to establish and implement appropriate strategies and to ensure an effective governance of risks in all areas of the bank." The 1st note states that "An adequate diversification, even in terms of age, gender and geographical origin, among other thing promotes the diversity of approaches and perspectives in analyzing problems and in taking decisions, Furthermore, to Sect. IV: In qualitative terms, the proper performance of the functions requires that in the organs with the strategic supervision and management are present subjects: with widespread skills between all the components and appropriately diversified, so as to enable that each of the components, is to ' of the Committees of which a part in that collective decisions, will actually contribute, among other things, to establish and implement appropriate strate-gies and ensure effective governance of risks in all areas of the bank. " Note 1) states that "Adequate ade-quate degree of diversification, even in terms of age, gender and geographical origin, among other things promotes the diversity of approaches and perspectives in analyzing problems and in taking decisions, avoiding risk behaviors mere alignment with prevailing positions, internal or external to the bank. Diversification can lead to a more intense level of involvement of each component on matters or decisions related to their own characteristics and. This should not undermine the principle of the active participation of all members in the work and decisions of the Board; each component must then be able to analyze and judge all the matters dealt with and all the decisions taken.

[10] Sector in which, for too long, women have been intended for secondary tasks and not even called to exercise executive functions and/or responsibilities.

[11] See MACCOBY and JACKLIN, *The psychology of sex differences*, vol. II, Standford University Press, 1974.

[12] On this matter, see among others MORERA, *Sulle ragioni dell'equilibrio di fenere negli organi delle società quotate e pubbliche*, su http://www.associazionepreite.it/scritti/morera006.php

[13] See MORERA, *Sulle ragioni dell'equilibrio di fenere negli organi delle società quotate e pubbliche*, which quotes the studies by BRIZENDINE, *Il cervello delle donne*, Milan 2007; ID., *Il cervello dei maschi*, Milano 2010.

[14] See BIANCO, CIAVARELLA and SIGNORETTI, *Women on Boards in Italy,* in *Quaderni di Finanza della Consob,* 2011, p.7, on www.consob.it.

[15] Article 36 of L. Decree 201/2011 (so called "Salva Italia" Decree), implemented by Law no. 214/2011, has introduced the ban of accepting or exercising roles between companies or groups of competitor businesses within the credit, insurance and financial market (so called "interlocking ban"). If those who hold incompatible roles don't choose one of the possibilities within the set date, they lose both their positions. In the event of total indifference, the loss of their positions is pronounced by the Competent Authority.

To clarify the rules for the application of the ban and resolve any doubts of interpretation emerged with the new standard, the supervisory authorities whose responsibility is to ensure its compliance (Bank of Italy, Consob and Isvap now Ivass, in coordination with the competition and market authority) have shared and made public the criteria which will be used for the examination the situations provided by art. 36 (see. Document of 20th April 2012, available on the Bank of Italy website at http://www.bancaditalia.it/vigilanza/att-vigilanza/accordi-altre-autorita/accordi-aut Italian / interlocking/Criteri_div_interlocking.pdf and the relative explanations). The same authorities have subsequently defined in a memorandum the criteria and modalities to coordinate the activities and procedures for the analysis of interlocking situations and the possible revocation of the incompatible offices, especially with regard to cases where crossed roles involve the responsibility of several authorities.

[16] And if it is true that the companies in question must commit to recruiting more women, it is equally true that the labor market must be able to respond adequately to this effort. In other words, the broad debate on gender parity from the perspective of the enterprise, must be accompanied by an adequate reflection on the fact that women are not always ready to respond to market demand.

If the demand for labor does not change it is likely to witness a process that in recent times, more than ever, has been avoided for all (men and women), that is a combination of roles and the repetition of names and people in the various board of directors; eventuality that certainly must be avoided. And that's not good. One way to change the demand on the labor market could be, as in other fields, through information and training; see. RINALDI and TODESCO, *Financial literacy and money attitudes: do boys and girls really differ? A study among italian preadolescents*, in Italian journal of sociology of education, vol. 11, n.2, 2012, p. 143 ff.

[17] 2014/95/EU Directive of the European Parliament and of the Council, 22nd of October 2014, amending Directive 2013/34/EU for that concerning the communication of information of non-financial character and of information on the diversity by certain companies and large groups.

[18] Action Plan, 2012

[19] See AZZOLINI, *Dopo le quote rosa, la gestione dei talenti*, on http://www.lavoce.info, 2015.

[20] See ROSSI, in CALVOSA and ROSSI, *Gli equilibri di genere negli organi di amministrazione e controllo delle imprese*, in *Osservatorio dir. civ. e comm.* , 1/2013, p.7.

[21] The nomination committee supports bodies with strategic supervision and management functions in the following processes: – appointment or co-optation of directors as specified in paragraph 2.1. With reference to the need to ensure an appropriate diversification in the composition of the collective body, the Committee – without prejudice to the obligations set by the regulation of listed banks (12) – sets a target for the shares of the less represented gender and prepares a plan to increase this value up to the set goal (The identified gender target, the plan and its implementation shall be disclosed as part of the information that banks must give accordingly to the "third pillar" (see. CRR, art. 435).).

Section VII: Disclosure Obligations. Banks, in addition to the information obligations arising from the EU provisions and the prudential rules of the Bank of Italy, disclose in a clear and detailed way and see to the constant updating of the following information: … – Total number of components of the governing bodies in charge and motivations, analytically represented, of any excess revenue in comparisson to the guidelines of Section IV. Distribution of the components at least by age, gender and duration of charge. …

The information to be published on the bank's website, including the information on the structural organization and corporate governance guidelines, can also be disclosed through the reference to other documents available on the website itself, including the Statute, provided that the information material is available and accessible through an accurate and clear link.

[22] See. Gender Quotas in management boards, 2012

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«They say things are happening at the border, but nobody knows which border» (Mark Strand)

# How motivation brings to healthy organizations: methods and incentives to increase satisfaction, efficiency and productivity

by **Angela Domenica Frusciante, Mohammed Elshendy** and **Nunzio Casalino**

**Abstract:** Motivation is a process consistent of several factors that make employees continually interested and committed in their job: it is done by stimulating their unique characteristics and their own needs/energies. Dealing with a managerial context, this article provides a wide discussion about the different keys that encourage motivation and empowerment; business well-being happens by adopting the appropriate strategies aimed at achieving satisfaction and productivity. There is a focus on intrinsic/extrinsic motivation and on how it is related to effectiveness, efficiency, productivity and performances. So monetary incentives are not always the right stimulus when the purposes are corporate healthy behaviors and high results. Furthermore, S.M.A.R.T. goals setting is explained: its implementation requires management-based theories and reinforcement procedures. In addition, leadership styles play an important role in this framework. The ones here discussed are participative, supportive and directive. The articles ends with a discussion on authors' findings and thoughts.

**Summary:** 1. Introduction. – 2. Role of motivation and organizational theories. – 3. The pyramid of needs and work dimensions. – 4. Goal settings and reinforcements. – 5. Leadership and motivation management. – 6. Research findings. – 7. Conclusions.

1. This article focuses on the useful factors for effectively motivating workers in their workplaces. A motivated worker generates value for the company. A good manager, therefore, is interested not only into the employees' physical health but also into the mental health, because this last is able to bring the highest results. The social changes of the 70s introduced an important new concept: health is not a factor to be taken into account when it is missing, but it is useful to implement policies in order to have a good climate in the organizations; this leads to study the psychosocial aspects of work [1]. It was increasingly evident the influence on health of both biological and psychological factors (as well as the importance of their combination and interaction). In the 90s the situation improved with the creation of the Occupational Health Psychology (OHP), an interdisciplinary topic aimed at optimizing the

quality of the working life and safety. In this perspective, healthy work environments are characterized by high productivity, good employee satisfaction, good security, lower absenteeism, few turnover and no violence. The OHP intervened on three basic dimensions: the working environment, the individual and the relation work/family. Raymond, Wood and Patrick (1990) [2] presented an assessment tool of organizational health-based indicators built considering two criteria: the time characteristic of the indicators (current, retrospective, and forecasting) and the availability/fluency of collecting data. A second study [3] aimed to a long-term view: a healthy organization is evaluated not only through the ability of working effectively but also through the ability to grow and develop. Consequently, the organizational health can be considered as the overall scenario and it is linked with studies on corporate culture and stress. The indicators of organizational "malaise" (symptoms) were spotted: this including the decrease in profits, the decrease in productivity, the absenteeism, the stress level of employees/organization and the overall well-being [4][5]. Avallone believes that the concept of organizational health is uncertain, generic and does not allow to identify the conditions by which an organization is in a good state and is able to keep it in time with motivation and productivity [6].

2. A lot of researchers addressed the aspect of motivation at work analyzing the factors that take place from job satisfaction and job dissatisfaction. The motivation at work can be defined as the inner drive that leads individuals to apply with energy and enthusiasm. It is a kind of internal strength [7] that stimulates, regulates and supports the major actions (taken by the subject involved) and can be described in a cyclic way: the individual searches for the tools in order to satisfy his/her own need, perceived as an inner tension; when it is satisfied, the subject checks for new and additional needs. Motivation is inside the individual and cannot be induced from the outside. Through external interventions it is possible to urge or, at most, to fuel it.

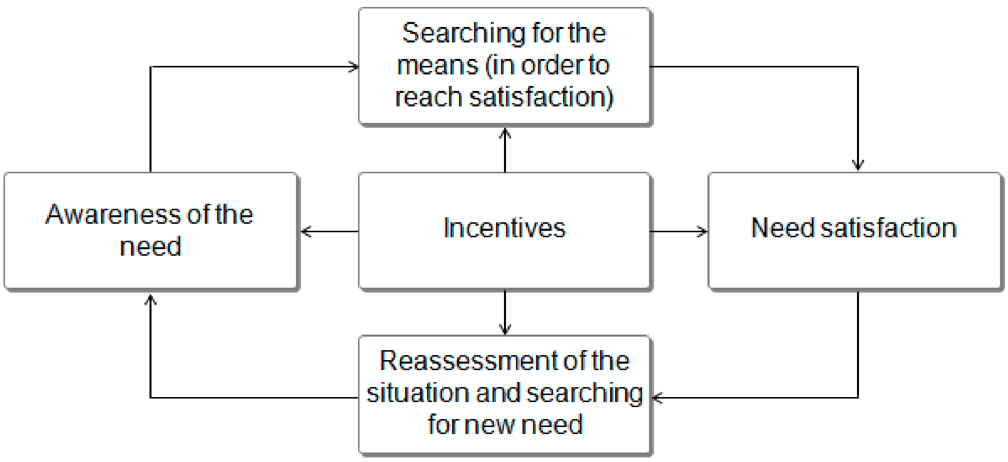


Figure 1: The life cycle of needs

The motivational system can be understood as the set of perceived needs and the links between them and the behavior. In order to define which are the elements that govern the motivation, several theories were formulated. For example Herzberg, in his studies, asked to the examined subjects to list what events in their professional life had caused satisfaction and what events had caused dissatisfaction [8][9]. The analysis of the results showed that the factors mostly contributing to generate satisfaction were related to the content of the work, while the factors of dissatisfaction were embedded in the working environment and remuneration. He took its cue from these analyses to develop a theory based on the distinction between two major classes of factors. On one hand there are those related to the external conditions of working such as the physical environment, social environment, remuneration (the ones that Herzberg calls the "hygienic factors"). On the other hand, there are the factors that affect the internal content of the work, and therefore the ability to provide a psychological growth for the worker (the ones that Herzberg calls the "motivational factor"). Herzberg thesis is that hygienic factors cannot provide an effective satisfaction. The improvement of hygienic or environmental factors (i.e. more wages or more comfort) can only lead to a lower dissatisfaction. Therefore, with particular regard to the link between man and work, Herzberg said that people can be classified according to two different basic attitudes: there are "researchers of motivation" and there are "researchers of hygiene". The people in the first group are not only interested in economic well-being, safety, comfort of the physical environment or the pleasantness of the co-workers. Their aim is reaching a high level of satisfaction at work that will give them the joy of a psychological growth. Researchers of hygiene, instead, are captured only by the external aspects of working such as remuneration, environment, etc. Herzberg also said that only the researchers of motivation can experience a real job satisfaction. So researchers of hygiene, although may declare themselves satisfied, are actually "not-dissatisfied". According to Frederick Taylor (Monistic Theory) the motivation of the employee must be stimulated through systems designed to maximize productivity: the solutions he proposed concerned the introduction of piecework, the profit sharing and the participation in the savings. These systems are called monistic and the aim is to ensure that each employee uses, at work, all his/her energy in order to maintain and increase productivity [10]. By increasing productivity, the employee can increase his/her salary, his/her self-esteem and his/her status. Motivation procured by money however is questionable. In order to increase motivation, in an enterprise context, it could be useful to introduce [11]:

- empowerment;
- job enrichment & enlargement;
- job sculpting.

The term empowerment has had in recent years a significant resonance: it has Anglo-Saxon origin and a set of multifaceted meanings. Empowerment means "increased power". On an individual level, it is the ability of people to feel responsible/protagonists of their own tasks and to expand themselves; on an organizational level, it is the opportunity for the company to be more effective in operations and innovative challenges. In both cases, however, the assumption in that everyone has the resources that may be developed. Job enrichment, instead, is the approach by which the characteristics of the work are modified in order to make employees work with more autonomy and responsibility. This process is called vertical job loading and it introduces new and more enriched activities that do not belong to the daily routine. The horizontal job loading, instead, introduces an enlargement of the job, incorporating activities belonging to the same organizational level (in this way, however, the change is only quantitative and will lead to a greater load of routine activities). Some of the basic job dimension are [12]:

- variety of tasks;
- clear identification of tasks;
- significance of tasks;
- autonomy;
- presence of feedback.

Job sculpting is “the art of retaining your best people” [13]. It consists in making workers exactly do the tasks they really want and on which they perform better, satisfying so their deepest desires.

3. The Theory of Needs argues that the behavior of a person, even at work, tends to the satisfaction of needs arranged in a clear hierarchy, which he has shown in a pyramid. Starting from the bottom, the following categories are registered:

- physiological needs, linked to immediate survival (breathe, drink, eat, relax, move);
- security needs, physical and emotional, related to long-term survival (freedom from danger, threats and deprivation caused by physical damage, economic hardship, illness);
- need for love and belonging (emotional relationships, acceptance by peers, recognition as a member of the group);
- need for esteem and self-esteem (recognition by others and self-respect);
- need for self-realization.

The individuals’ behavior is designed to satisfy the needs in the lower level, whose satisfaction leads to make them motivated and brings out the needs in the superior levels. This theory was very important in the management context during the last century, but it has some problematic sides: each individual, in fact, differs from the others and warns and meets the needs in different ways. For example, while some people are able to rest only a few hours’ sleep, others need many more hours; while some people want to eat when hungry, others tend to satisfy higher needs. Salvemini has defined a different scale of needs that an individual can experience in the work contexts. The rank is:

- consumption needs;
- security needs;
- needs of sociability;
- esteem needs;
- power needs;
- needs of realization.

According to this author the satisfaction of a need, defined as the lack of a desired object, can be functional or dysfunctional to the satisfaction of other needs (i.e. the fulfillment of the desire for power can be functional to the needs for self-realization). According to Vroom (1964) [14], instead, motivation is related to two factors: the value, which is referred to the importance that one person gives to the achievement of a goal, and the expectation, which is represented by the probability recognized in order to achieve it. Motivation is so expressed in this formula:

$$\textit{Motivation} = \textit{Valence X Expectancy}$$

The value can be positive (when you want something) or negative (when you don’t want something), while the expectation can only have positive value in fact, if the person doesn’t recognize any chance of achieving the goal, the expectation is equal to 0. This theory was further developed and was enriched with an additional factor: the value of the reward, which refers to the reward of achieving the objective. The formula becomes the following:

$$\textit{Motivation} = \textit{Valence X Expectancy X Value}$$

According to this principle, the motivation of staff can be defined as a function of the work done, the objectives achieved and the behavior (i.e. if the behavior is considered positive, such as high performances at work, it should be subjected to a premium). The level of needs' satisfaction generates the organizational structure and the corporate climate/culture. The organizational behavior, that affect the individual performances, is the result of the interaction of four dimensions:

- extrinsic dimension (A);
- intrinsic dimension (B);
- dimension of sociality (C);
- dimension of solidarity (D).

A) *Extrinsic motivation* follows when an employee engages in an activity for purposes that are extrinsic to the activity itself, such as, for example, receiving praise, recognition, good grades or avoiding unpleasant situations, as a punishment or a fool.

B) *Intrinsic motivation*, in contrast, occurs when a worker engages in an activity because he finds it challenging and rewarding, feeling more and more competent. Intrinsic motivation is based on curiosity, which is activated when an individual meets environmental characteristics as strange, surprising and new; in this situation the person tends to explore the surroundings in order to search new information and solutions.

C) *The dimension of sociality* refers to the degree of friendship between the members of a community. There are many benefits: creativity is rewarded, work environment is pleasant, trust and mutual respect are produced. Pay attention to avoid the groupthink phenomenon, where consensus takes the place of the constructive debate and criticism.

D) *The dimension of solidarity* finally regards the actual interests / goals of the people. Solidarity determines a significant focus on the objectives, produces intolerance for unsatisfactory performances and allows you to respond quickly to threats. As disadvantages: the level of cooperation depends only by mutual interest and, if the roles are strictly defined, disagreements could arise inside the group.

Goffee and Jones' (1999) matrix [15] explains the relations between the last two dimensions.

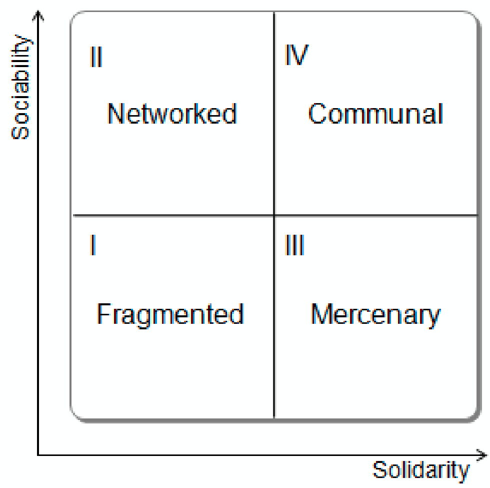


Figure 2: Goffee & Jones' Matrix

The box related to the "fragmented" concerns with the workers who interact with low sociability and little solidarity: goals are not perceived and interpersonal relationships are not present (sometimes it could happen that employees work remotely and they do not know each other). People in the "networked" box upgrade friendly relationships but are not so interested into sharing common objectives and tasks. The third box ("mercenary"), instead, has a strong focus towards the goals: typically these communities have short live and are highly motivated in the achievement of specific goals (i.e. Soldiers, Project Work Teams; even if the work experience is finished, during the time, the period spent together is remembered nostalgically and with pleasure). The ideal organization is the organization of citizens ("communal") [16] where the degree of sociability and the degree of solidarity are both high: the persons are strongly motivated into achieving their professional tasks, sharing suggestions, observing deadlines, partaking into meetings and, in the same solution, into establishing social relationships rather hardly (sometimes co-workers become good friends and they also meet each other after work for informal drinks).

4. Goals are defined as the desired future conditions that the organization intends to achieve. Therefore, considering that these conditions are focused on company's purpose, the way they are being achieved is very important. Goal setting is a crucial dimension for labor relationships and it has been studied in fields such as Psychology and Economics [17]. According to the management and organizational literature, in order to motivate workers, one of the leader key-tasks is to promote clear purposes and ambitious goals for the whole team. A recent Fortune report talked about "Why CEO's fail" and estimated that projects execution failed in 70 percent of organizations, due to [18]:

- managers' disability to create a balance between strategic and operational tasks;
- unclear goal setting strategies.

Meanwhile, in Psychology literature, it is well recognized that goal setting is an effective way of achieving behavioral change in people. For instance, many psychologists argue that wage-irrelevant performance goals enhance employees' motivation and work performance [19]. Goals should be relevant (according to the person involved), challenging but realistic, achievable, specific and measurable [20]. According to this topic, in the last years one question arose: "How should goals be specified or written"? Locke and Latham carried out a case study explaining that employees are motivated when clear goals and periodic feedback (these last ones regarding performances) are provided. Their conclusion was that specific and precise goals have the highest motivational effect rather than vague and easy ones. Later, they developed five fundamental principles in order to create effective goal setting: the S.M.A.R.T. goal system [21]. S.M.A.R.T. goal setting drives towards efficacy. Instead of vague targets, SMART goal setting creates prosecutable path towards certain objectives, precise milestones and reliable results. Every goal, from the easiest to the most difficult one, can be made S.M.A.R.T. [22]. The acronym S.M.A.R.T. means:

- Specific – what is being pursued is exactly defined;
- Measurable – the achieved results are measured using recognized indices;
- Attainable – the goals are realistic to be achieved;
- Result – the goals are result-oriented;
- Timely – the milestones are exactly fixed in the timeline.

Reinforcement theory for motivation was proposed by Skinner and his colleagues. This theory said that the individual behavior follows the "law of effects". For example, individuals tend to repeat the actions that reproduce positive consequences and eliminate those ones that drive toward negative effects. Thus, according to Skinner (1953) [23], the organization must design its environment in order to encourage workers toward positive consequences. This theory is useful to control and analyze the different mechanisms concerning the individual behavior. The reinforcement is the submission of a certain kind of temporally limited stimulus which produces a response [24]. A reinforcing stimulus is defined by its power and by its ability to produce the desired changes. Some stimuli are able to produce changes, better than others are, and, consequently, they are classified as reinforcing or no reinforcing. Reinforcement is fine when the positive behavior increases or maintains its frequency. In the organizational context, the employee desires the reinforced signal if he/she associates the outcomes to the behavior; in these cases the effect is stronger, more resistant and difficult to eliminate. In reinforcement learning, the procedure of selecting the best action is based on evaluating the results achieved during the observations (it could be useful to conduct many tests in order to individuate the best reinforced signals to use). The leader will choose the action, which maximizes the desired results [25]. Leaders use the following methods aimed at enhancing employees' behavior:

*Positive Reinforcement* – It implies giving a positive response when the worker shows the right and required behavior (i.e. immediately praising an employee for coming early at work). This will increase the probability by which the behavior occurs again. Rewarding, for example, is positive but not in all contexts. Only if the employees' behavior improves, rewarding can said to be a efficacious. The greater reinforcement happens when the intention of giving a reward is spontaneous.

*Negative Reinforcement* – It implies dealing with an employee by using action aimed at removing negative/undesirable consequences. Both positive and negative reinforcement can be used for increasing desirable/required behavior. Negative reinforcement is often used if positive reinforcement have not been effective in increasing the target skill/behavior [26].

*Punishment* – It implies removing positive consequences in order to decrease the probability by which an undesirable behavior befalls. In other words, punishment means applying undesirable consequence aimed at forbidding undesirable behavior (i.e. suspending an employee for breaking the organizational rules). In such contexts, considering the gained results, punishment can be equalized to positive reinforcement.

*Extinction* – It happens when reinforcements are absent. So extinction aims at lowering the probability of occurred-undesired behavior by removing all kinds of rewarding (i.e. if a worker no longer receives praise and admiration for his/her good work, he/she may feel unappreciated for his/her contribution). Extinction may unintentionally reduce desirable behavior.

5. Several studies have shown that leadership styles and motivation are strictly related: the most motivated followers have the most motivated leaders and vice versa [27]. According to this trail, the most important factors that an organization should use in order to preserve its effectiveness and its productivity are joined to the different leadership styles. Researchers have defined numerous and different leadership styles. The "style of a person" is created through the combination of his/her beliefs, values and preferences, organizational cultures and norms (encouraging one style and, even, discouraging others). As concerns Leadership Theories, there are three main key variables that affect the leadership styles: the leader's characteristics, the follower's characteristics and the environment's characteristics.

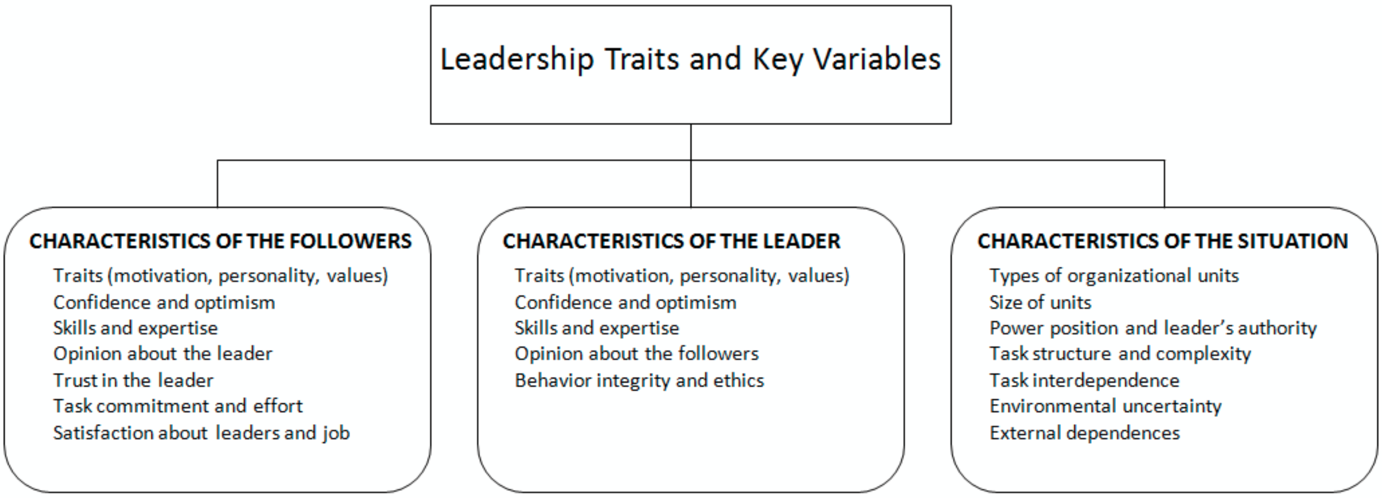


Figure 3. Key leadership components

*Participative leadership style*. It makes workers have high influence about their work decisions. This type of leadership leads to participative conditions where subordinates share a significant degree of decision-making power with their superiors. For example, if the workforce is smart, well-staffed and skillful, subordinates would prefer participative managers rather than directive ones. Instead of suppressing disagreement, aimed at appeasing the superior anger or ideas' divergence (as done in the recent past), the new generation of workers would definitely prefer to have a precise role in decision making. Supportive leadership style. It establishes a psychological support towards subordinates and this facilitate goal achievement, mutual trust and respect, helpfulness and friendliness. A channel leader with a supportive leadership style considers other channel partners' needs, looks after other partners' well-being, creates a pleasant atmosphere for interaction, encourages other units' accomplishments, looks out for their welfare, establishes mutual trust and builds a harmonious climate. Directive leadership style. It characterizes the leader that provides specific guidelines in order to drive his/her own subordinate work activities; this is managed by organizing and defining the task environment, assigning the necessary functions to be done, specifying rules and procedures to be followed (while accomplishing tasks), clarifying expectations, scheduling work, establishing communication networks and evaluating work group performance. Buble, Juras & Matic (2014) [27] said that motivation depends also on the following characteristics:

*Demographic characteristics*. They are relevant in order to configure managers' motivation and leadership styles. The most famous ones are those five: gender, age, academic degree, total work experience and work experience in the specific company.

*Communication*. It is commonly defined as the process of transferring information from one person to another. Interpersonal communication is not only the involvement grade of an individual in a group, but also the individual's self-realization level. Therefore, the communication development in the company significantly affects business performances and demonstrates the leadership style.

*Interaction*. It is the process of mutual and reciprocal influence regarding two or more people's behavior. Interaction has crucial importance for the management and it mainly bursts through the leader and his/her co-workers. It could be helpful to study the different kinds of interactions between the manager and his/her subordinates.

*Decision-making*. It is defined as the process of identifying the problems and the opportunities to resolve them [28]. It includes efforts before and after the decision is made. Who the decision makers are and how intensely the subordinates are involved in the decision-making process has a significant impact on the solutions' realization. Therefore, it is very important to examine how this process takes place in the particular companies.

*Controlling*. It is aimed at monitoring employees' activities, determining the way the company uses towards the goals established; if needed, it supports corrective decision-making [28]. The management task is to ensure that employees are focused on achieving the goals fixed. In the context of graduated organizational changes [29], empowerment and trust are developed following new trends (the workers are less self-governed equalized to the previous classifications).

Therefore, the riddle is: "Which combination of leadership styles, motivation and followers' satisfaction results optimal for the organizational effectiveness?".

6. Multiple researches have shown the great influence of leadership on motivation. For example Mehta and other (2003) [30], studied the workers' performances subjected to multiple kind of motivation created by different leadership styles. The research showed that participative, supportive and directive leadership styles return all high levels of performance. Wright and Pandey (2010) [31], Bass and Riggio (2006) [32] and Storseth (2004) [33] found that the people-oriented leadership style is a key predictor for work motivation. Many other researchers have also confirmed these results leading to the thesis that the relation between leadership styles and employees' motivation is strong. So, as a result, the following model shows five principles in order to increase business productivity:

1) optimize human resources. A reorganization of human resources makes people do the activities they really "fit". Knowing the potential of each member in the company and entrusting the right responsibilities will enhance efficiency [34];

2) spur interpersonal relationships between employees. Quarrels and negative situations significantly harm the productivity. Suggesting corporate learning [35], creating a serene atmosphere and organizing events after-work (such as dinners or lunches) will help collaboration and tolerance among colleagues;

3) stimulate motivation encouraging members to do the best actions and to improve their position within the company (i.e. offering financial incentives or reward, such as travel, dinners, certificates, esteem, etc.);

4) improve the employees' welfare providing adequate break (i.e. coffee break to recharge the forces and make no mistakes) and allowing more flexibility (i.e. part-time or working from home, after a period of illness);

5) define priorities and delegation drawing up a list of things to do. It could be useful I) to delete – from time to time – the activities carried out, II) to get no distraction from colleagues and III) to delegate less pressing and important tasks.

7. A successful organization can reach its success by motivating employees. However, it can be difficult; there are no magic formulas or programs helpful to do this. Motivation is a personal dimension. While one employee may appreciate time off, another may enjoy new

challenges. The basic rule is to discover what the workers want making it become reality or encouraging them to earn it. This is a success key for a department or a company [36]. Moreover, extrinsic factors are more significant compared to intrinsic ones. So high salary, job security, etc., are more frequently required by employees and have the bigger impact on their motivational behaviors [37] but factors such as getting recognition for a job well done are more precious than the previous. Both categories of motivation enhancers, considered in different mixes, are always present in all type of leadership styles. The researches' results have confirmed that the relation is stronger between intrinsic motivation and leadership style rather between this last and extrinsic motivation. In conclusion, influencing managers' leadership style to motivational factors is very important [38] to avoid the drift towards the authoritarian leadership which is very dangerous. General principles to adopt and to support employees in their work are: know effectively the staff, give useful feedback, encourage people in achieving the goals, educate about the "business well-being", keep them informed and involved with the GAOS (in Italian: Grande Audace Obiettivo Sfidante) and adopt rewards (such as verbal recognition, professional development or money). Without motivation, nothing really gets started, as what you pay is what you get.

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«They say things are happening at the border, but nobody knows which border» (Mark Strand)

# The voice of stakeholders in large corporations under the Italian legislation of the last 10 years.

by **Raffaele Lener**

**Abstract:** Following the reform of 2003, the Italian company law system is very open and flexible and is one of the most modern in Europe. Indeed, the Italian legislator envisages, on the one hand, shareholders that play no part in the management of the corporation and, on the other, non-shareholders that are instead granted administrative rights. While the assignment of administrative rights, including the right to vote, to non-shareholders is a frequent (indeed, almost common) occurrence in common law systems, it is considerably less so in continental Europe and, when it is allowed, there is an effort to restrict the non-shareholders' weight in the management of the corporation. The author tries to illustrate the new categories of financial instruments that an Italian corporation can issue, the corporate rights attached to these new instruments and the role that non-shareholders can now play in the governance of large Italian joint-stock corporations.



**1.** Giorgio Oppo's well-known comment, which provides the starting point for these brief notes, is that the modern *società per azioni* (SPA) may be described as an "open business structure" with a variable organisation. An organisation in which shareholders and non-shareholders may co-exist, there may or may not be the "profit-sharing purpose" envisaged by article 2247 Italian Civil Code and persons other than the shareholders may share the profits [1].

Although the flexible model of SPA introduced by the 2003 reform maintains certain "contractual" aspects, it would appear to be the result of a (more or less conscious) legislative choice to *interpret* the corporation as an *institution* [2].

The new relationship between shareholders and non-shareholders, the administrative rights that may be assigned to the latter and the possible reduction of the former's administrative rights without a necessary economic "readjustment" create a certain distance between the organisation and the *contractual model*.

Following the reform, the Italian system is very open and flexible and is one of the most *modern* in Europe. Indeed, as we shall see, the Italian legislator envisages, on the one hand, *shareholders that play no part* in the management of the corporation and, on the other, *non-shareholders* that are instead granted administrative rights.

In fact, the assignment of administrative rights, including the right to vote, to non-shareholders is a frequent (indeed, almost common) occurrence in common law systems[3]. It is considerably less so in continental Europe and, when it is allowed, there is an effort to restrict the non-shareholders' importance in the management of the corporation.

There are principally two, potentially alternative (in light of the experience in other countries), reasons for assigning non-shareholders such rights: either to allow stakeholders to play a part, where possible, in the management of the corporation or to grant them administrative rights as a way of protecting their investment. Both reasons apply in Italy and the law virtually gives articles of association *carte blanche* with regard to regulation. Articles 2346 and 2351 Italian Civil Code only reveal an intention to maintain the shareholders' primacy in the management of the corporation. However, as we shall see, the limits are not always clear.

**2.** We know that the articles of association are free to create any *categories* of shares and to attach different rights to them. The law provides no parameters and even the "limits" within which the articles are allowed to operate (pursuant to article 2348, paragraph 2, Italian Civil Code) are uncertain and not readily apparent[4].

Thus, *categories* of shares may be freely created. It is not, instead, possible to assign individual shareholders particular rights relating to the management of the corporation or the distribution of profits (as in limited liability companies). I would say that particular rights in SPAs must still be assigned on an *objective* and not individual basis. This is the manner in which the concept of "category" must be interpreted, even though the articles of association have an almost unlimited power to establish its boundaries.

As regards the "limits" imposed by law, there is a *quantitative limit* on the issue of non-voting shares, limited-voting shares (where the right to vote is restricted "to particular matters") or shares whose voting rights are conditional upon the occurrence of certain future events. The overall value of such shares may not exceed one-half of the share capital (article 2351, paragraph 2, Italian Civil Code).

Even the traditional prohibition on issuing shares with *multiple voting* rights (article 2351, paragraph 4, Italian Civil Code, prior to the reform) has recently been transformed into a *limit* – although this decision was adopted, with no careful consideration of the matter, under the emotive pressure of the government's emergency measures for the "growth of the country". Corporations may now issue shares carrying more than one vote, with a limit of three votes per share. However, listed corporations may not issue multiple voting shares (the *prohibition* still applies in this case), but they may, through their articles of association, *increase the number of* *votes* to a maximum of two per share for shareholders that have continuously held their shares for at least two years (new article 127-*quinquies*, Consolidated Law on Finance, introduced by the "growth" Decree, *Decreto Legge* no. 91 of 24 June 2014, converted into Law no. 116/14).

It is difficult to ascertain whether the system envisages additional limits or prohibitions.

Scholars (still) tend to rule out any possibility of shares with *particular rights to appoint* (outside the shareholders' meeting) corporate bodies[5], based – it would appear – on the assumption that votes expressed in the shareholders' meeting constitute the "typical and exclusive" way in which shareholders contribute to the management of the corporation's affairs[6].

There is also a debate on whether it is possible to issue categories of shares carrying the *right to veto* certain shareholders' resolutions. Those who argue against this[7] do so based on the principles which may be inferred from the prohibition on multiple voting shares and the restrictions on the issue of limited voting shares, which, they say, imply that the system wishes to prevent a situation in which control is given to a category of shares representing a minority quota of the share capital. However, this argument is not entirely convincing. If – as the more "liberal" scholars accept and as appears entirely reasonable[8] – it is possible to issue shares with the right to vote *on the authorisation of management decisions* pursuant to article 2364, paragraph 1, no. 5, Italian Civil Code, there is no reason why it should not also be possible to issue shares with *veto rights* on the same matter. At most, categories of shares having the right to authorise, or veto, the directors' management decisions could be equated to categories of shares with limited or conditional voting rights so that they would be subject to the overall limit of one-half of the share capital.

Article 145, paragraph 1, Consolidated Law on Finance does not appear to envisage any further limits on the creation of categories. This provision only allows the issue of non-voting shares ("*azioni di risparmio*") if the corporation has ordinary listed shares (on regulated markets, including in other EU countries) and provided that the lack of voting rights is *compensated* by economic benefits, although the law provides no criteria to define such benefits, leaving this task to the articles of association (article 145, paragraph 2, Consolidated Law on Finance). In effect, this article – which undoubtedly *goes against the current trend* – compensates for the rights which are taken away from shareholders (voting and associated rights) by giving them something in addition to the rights assigned to them by law (economic rights) and is, as such, an "old-style" provision that appears to have ignored the 2003 reform.

Indeed, the question is whether, in light of the new article 2351, paragraph 2, Italian Civil Code, categories of non-voting shares can be created without any form of economic compensation and without any requirement that the ordinary shares be listed. The answer must now be affirmative: "*azioni di risparmio*" do not account for all the categories of shares which may in theory be defined as *not carrying voting rights*. One could merely have the foresight to give them a different name: "*azioni senza voto*", "*azioni non amministrative*" and so on. This would eliminate the listing requirement and the obligation to provide economic compensation, leaving only the quantitative cap envisaged by article 2351, paragraph 2. In other words, only shares named "*azioni di risparmio*" are protected to avoid confusion.

Finally, a "systemic" limit may be inferred from the *prohibition on leonine agreements* pursuant to article 2265 Italian Civil Code (i.e. the exclusion from participating in profits or liabilities)[9], on which case law has recently placed new emphasis (e.g. Court of Milan, 30 December 2011, in *Le società*, 2012, p.1158). However, it should be noted that article 2348, paragraph 2, Italian Civil

Code allows different rights to be granted "including with regard to the impact of losses", so much so that there is an increasingly frequent use of subordination. Probably, the only practical consequence of the prohibition is probably that is possible to issue categories of shares which are entirely excluded from profit sharing.

It is clear, then, that there are very few "statutory limits" on the creation of categories. As a consequence, the principle, envisaged by article 2348, paragraph one, Italian Civil Code, that all shares are equal – which has been downgraded to equality *within* the category – ultimately has very little meaning. Indeed, it could even be removed entirely were it not for the fact that the market still requires that shares with the same content belong to a category with a certain *name*.

In conclusion, there may undoubtedly be shareholders who contribute to the capital, but have *no administrative rights* in the management of the corporation and do not necessarily receive enhanced economic rights to offset this loss.

As a result, it is increasingly difficult to think of shareholders – only or mainly – as parties to a corporate contract [10]. Indeed, from a contractual perspective, although there is no requirement for the shareholders to be absolute equal, there would have to be a causal justification for any inequality and, thus, a *reasonable equilibrium* between the shareholders which in return for the sacrifice of certain individual rights envisages the enhancement of other rights. This "need for equilibrium" is no longer recognised by the system that currently governs *SPAs* [11].

The final reason for allowing such contractual *imbalances* most probably lies in the legislator's desire to guarantee that corporations have access to as many sources of funding as possible, so that they are no longer exclusively dependent on funding from banks.

Corporations need funding and they are allowed to raise funds even by issuing shares with no administrative rights, just as they are also permitted to issue financial instruments other than shares which, as such, do not represent equity interests, but which may carry administrative rights.

Ultimately, the market will be the final judge. It is clear that there will be no market for an *imbalanced* category of shares, i.e. one in which the administrative penalisation is not offset by an adequate economic benefit – which, as mentioned, is permitted by law regardless of the reaffirmation of the principle of equality – and so it will not enable issuers to raise funds. Moreover, the protection offered by the special shareholders' meeting envisaged by article 2376 Italian Civil Code will not apply since this remedy only operates against the *worsening* of the terms of issue and is ineffective against inherent penalisations of the category.

These considerations appear to confirm that the general rationale behind the reform of 2003 is that (small) shareholders are viewed as *investors*, who use their savings to fund businesses managed by others. As a result, the emphasis is on the financial aspect of the contribution in light of the SPAs' *natural vocation* to raise funds on the risk capital market. Moreover, from this perspective, it is of *no interest* to the legislator whether an investment is defined as a contribution (*conferimento*) or as a consideration (*apporto*), or whether an investor is defined as a shareholder (although not a controlling shareholder, of course) or a creditor with a (limited) voice [12].

**3.** The contractual rights of shareholders are further reduced by the presence of third-party rights, i.e. held by non-shareholders, *with management powers.*

Article 2346, paragraph 6, Italian Civil Code allows corporations to issue financial instruments that carry economic "or also administrative rights, excluding the right to vote in the *shareholders' meeting*" against consideration, by shareholders or third parties in general, in the form of work or services. Such consideration "does not constitute a contribution and does not contribute to or increase the corporation's equity"[13]. The articles of association regulate the procedure for their issue and their contents and, if transferrable, also the relevant law.

This provision opens the way to a panoply of cases, which are perhaps in some respects even more numerous or, in any case, more *flexible* than the *categories of shares*, whose limits do not apply to the instruments which we shall call "participating instruments".

There is no mention of *categories* of (participating) financial instruments, which suggests that it may be possible to issue *individual securities*.

Notwithstanding the great uncertainty arising from the meagre provisions of the Italian Civil Code, it would appear that individual issues are possible. Indeed, the rules on special meetings set forth by article 2376 Italian Civil Code also mention participating financial instruments, but the provision states: "*if* there are different *categories* of [shares or] financial instruments that carry administrative rights". Thus, it is reasonable to assume that, where a category of participating financial instruments exists, there must also be a (special) meeting of the category. However, if individual securities are issued, there will clearly be no meeting of the category. In this case, the (only) remedies available to individual financial instrument holders who are damaged by a corporation's decision will be the general remedies envisaged by statutory law.

**4**. It is not easy to identify the administrative rights that can be assigned to the holders of such instruments.

There can be no doubt that participating instruments may carry *information rights*; for example, the right to consult the corporation's books, request information, postpone meetings due to insufficient information and also the powers envisaged by article 2408 Italian Civil Code. From this perspective, holders may perhaps be allowed to *attend but not intervene in shareholders' meetings*, but this raises issues of compatibility not so much with article 2346 as with the new version of article 2370 Italian Civil Code and the apparently necessary connection between attendance and voting[14].

The issue of *rights of participation* is more complex.

In fact, as mentioned, the provision allows the generic assignment of *administrative rights*, which will be determined by the articles of the corporation, with the sole limit that such rights will not include the right to "vote in the general shareholders' meeting". It must be said that "administrative right" is merely an "*a contrario*" definition: any right that cannot (exclusively) be classified as an "economic right" will be defined as an administrative right. Actually, the law even fails to define the concept of general shareholders' meeting, but, once again, the definition can be inferred *a contrario* from article 2376 Italian Civil Code: a general shareholders' meeting is a meeting not intended for individual categories.

Financial instruments may be assigned administrative rights and economic rights, or even just administrative rights. The phrase used by the legislator is not particularly clear ["carrying economic rights *or even* administrative rights"] and suggests that such instruments must always assign economic rights and may, exceptionally, *also* assign administrative rights. However, I can see no systematic reasons for ruling out instruments that only assign administrative rights. In a case such as this – which is probably destined to remain in the realms of theory – it should be possible to transfer the financial instruments so that the holder can (at least) make a profit from their sale.

**5.** The prohibition on voting in general shareholders' meetings is not easy to interpret in light of article 2351, paragraph 5; indeed, there appears to be a clear lack of coordination between the two.

Article 2351, paragraph 5 provides that participating financial instruments may carry the right to *vote on specifically indicated matters* and, *in particular,* they may be assigned the right to appoint an independent member of the board of directors or supervisory board or a statutory auditor.

In effect, these provisions are irreconcilable without partially emptying the prohibition contained in article 2346 of *technical* meaning and transforming it, within the limits that we shall see, into a general statement of principle.

Indeed, any interpretation of article 2351 that limits the voting rights of financial instrument holders to special meetings is unacceptable[15]. When the law mentions "vote" without further specification, there can be no doubt that it is necessarily referring to the (general) shareholders' meeting. Moreover, there would be no reason to expressly assign the right to vote in the special meeting given the provision of article 2376 Italian Civil Code. Furthermore, since the right to vote in the special meeting serves to protect the rights of the *category*, there is no way it could be limited to "specifically indicated matters".

Similarly, voting cannot be reduced to a mere *declaration of an opinion.* If the intention had been to provide for consultation of the financial instrument holders, the legislator should not have used the word "vote".

Nor would it make any more sense to interpret the provision as if it referred to the *appointment outside the shareholders' meeting* of members of the corporation boards: article 2351 envisages the assignment of the right to vote, which is a right that is typically exercised at the shareholders' meeting.

Moreover, the fact that the holders of these instruments are not prohibited from taking part in the "general" shareholders' meeting is demonstrated by a – better-worded – provision which expressly states that even cooperatives may issue participating instruments. Indeed, article 2526, paragraph 2, Italian Civil Code provides that "financial instrument holders may not, in any case, be assigned more than one-third of the votes granted to the total number of shareholders present or represented *at each general meeting*".

As for the specific matters on which these persons may be entitled to vote, all that can be said at present is that such matters must fall within the competence of the shareholders' meeting and not within the remit of the directors.

Instead, it is correct to assume that the scope of the "specific matters" on which participating instrument holders may vote must not be such as to encroach *in general* on the voting rights which are *reserved in principle to the shareholders* (which is the *real meaning* that should be attributed to the provision of article 2346, paragraph 6): thus, it is *not* so much a prohibition on *voting in the – general – shareholders' meeting* as a *prohibition on attributing a general scope* to the voting rights of the participating financial instrument holders[16].

Therefore, the exclusion of voting rights in the "general shareholders' meeting" should be interpreted not with reference to the body, but to the general nature of its areas of competence, which is replaced by the specific indication of particular matters.

Lastly, it should be emphasised that the law does not introduce a rule of proportion with the vote of shareholders, so that where there are both voting rights attached to shares and voting rights attached to financial instruments during a "general" meeting, the articles of the corporation will have to adjust the "weight" that each carries (with criteria that are, however, difficult to establish since, as we have seen, the contribution of works or services is also freely permitted).

**6**. The member of the management[17] or supervisory board who may be appointed by the holders of participating instruments must be regarded as having full powers and not as being a "quasi director" or "quasi auditor". The only provision is that he or she be "independent", i.e. meet the statutory requirements of *independence* (those envisaged by article 2399 Italian Civil Code or any others applicable), but we also cannot rule out that she or he may have "executive" powers. At least, this is the case in the traditional and in the one-tier system, since the two-tier system does not envisage the appointment of a member of the management board. Once again, there is a certain lack of refinement on the part of the legislator.

The provision does not even clarify whether, if there are several categories of financial instruments, the articles may assign *each of them* the power to appoint an independent director or auditor; nor does it clarify whether, in such case, there is still a cap on members not elected by the shareholders. Again, a legislative gap of no little importance.

It is clear that the interpretation whereby the majority of the members of the corporation boards must necessarily be chosen by the shareholders is not fully convincing with regard to a flexible organisational model such as that of "modern" SPAs. Besides, it would not be easy to find a legal basis.

The only argument that may, perhaps, be used to define the scope of the power to appoint corporation bodies that may be attributed to financial instrument holders is the formal argument that may be inferred from a strict interpretation of article 2351, paragraph 5, where it provides that "the appointment of *an* independent member may be reserved to them, in accordance with procedures established by the articles of association, (…)". This would imply that the total number of such independent representatives could not exceed one, with the consequent need to establish unitary election mechanisms in cases in which there are several categories of financial instruments[18]. However, any argument based on a literal interpretation is undoubtedly somewhat weak when the provisions in question are so unclear and incomplete.

**7.** As mentioned, another issue is whether the financial instruments may be attributed the right to *attend* the shareholders' meeting, since article 2346 Italian Civil Code *only* excludes – in the manner specified – their *right to vote*. If this were the case, there would be a conflict with article 2370, paragraph 1, Italian Civil Code, which provides that only "those who are entitled to vote" may attend the shareholders' meeting. The issue is, naturally, of general relevance. However, in this case, one could even adopt the broadest interpretation, given the importance – from the perspective of their information rights – of the financial instrument holders' attendance.

There is also an issue as to whether the participating financial instrument holders are entitled to challenge resolutions, naturally only regarding matters on which they are entitled to vote. In fact, article 2377 *only* refers to challenges *by shareholders*, but one could perhaps try to overcome this formal limit based on the logical connection between vote and challenge. However, I believe that, *in general terms*, this suggestion should be rejected due to the insurmountable technical problems that would arise: if nothing else, just consider the practical impossibility of applying the minimum shareholding requirement envisaged by the third paragraph of article 2377.

Therefore, it is reasonable to assume that, where there is no provision in the articles, a financial instrument's voting right *does not imply*, by default, a right to challenge. However, there is no reason why the articles should not envisage such a right – indeed, the articles may certainly derogate from the aforementioned quantitative limit – and, in this case, regulate the relevant procedure and, in particular, the entitlement criteria.

**8.** In addition to the general provision of article 2346, paragraph 6, Italian Civil Code, which has, as we have seen, an *open* content, Italian company law envisages other – what we might call – special participating financial instruments with a *partially predetermined* content.

I should specify that the financial instruments *assigned to workers,* envisaged by article 2349 Italian Civil Code cannot be considered *special*, as the only thing that differentiates them from the general type of financial instruments is that they are issued to employees of the corporation. Nor should financial instruments issued by cooperatives, pursuant to the aforementioned article 2526 Italian Civil Code, be considered *special* for our purposes, since they also fall within the general provision (which are expressly referred to in the first paragraph of article 2526), with the only specific provision being the withdrawal right of holders of instruments carrying voting rights, in accordance with the procedure envisaged by article 2437 Italian Civil Code (article 2526, paragraph 3).

There are two genuinely "special" types of special participating financial instruments.

The first is that envisaged by article 2411, paragraph 3, Italian Civil Code, which extends the rules on bonds "to financial instruments, howsoever named, which make the timing and extent of the repayment of the capital to the economic performance of the corporation". In this case, the provision clearly envisages *quasi debt instruments* and not "corporate" instruments[19].

The second special type is envisaged by article 2447-*ter*, paragraph 1, letter (e), which refers to financial instruments for "participating in the transaction", which the corporation may issue when it resolves to set up a dedicated fund, with a "*with a specific indication of the rights conferred by such instruments*". It appears that the articles of association may only assign supervisory powers to such instruments and not – at least, in principle –administrative rights: holders should *not* be able to play a role in the management of the transaction (based on article 2477-*ter*, paragraph 1, letter (d) and article 2477-*octies*, paragraph 1, no. 1, Italian Civil Code). Even the special meeting envisaged by article 2477-*octies* is not that referred to in article 2376 Italian Civil Code, but is equivalent to the bondholders' meeting envisaged by article 2415 Italian Civil Code (the rules of which are expressly referred to).

The relationship between the general and special participating financial instruments is ambiguous. In particular, there is debate as to whether such instruments may also carry administrative rights. The simplest solution is that they may not, since the *relationship* between the two sets of rules is one *of mutual exclusion and not complementarity* (that of article 2411 and those of article 2346 and article 2477-*ter*)[20]. As we shall see, this is true in part.

There can be no doubt that "quasi debt instruments" have their own set of rules, which is that applicable to bonds, and this distinguishes them from the "general" participating financial instruments envisaged by article 2346 Italian Civil Code. The specific rules regard three aspects: (i) the quantitative limit on their issue (i.e. double the share capital pursuant to article 2412 Italian Civil Code), which only applies to *quasi debt instruments*; (ii) the procedure for their issue: a board of directors' resolution is sufficient for *quasi debt instruments* (pursuant to articles 2410 and 2411, paragraph 3 Italian Civil Code), while article 2346 requires provision in the articles of association, with no need for a subsequent shareholders' resolution if the articles already provide all the details (procedure, conditions, issue, content of the rights, specific provisions for non-fulfilment and, if transferrable, also the relevant law); the articles could certainly delegate such matters to the shareholders' meeting or the board of directors, but the source would still be the articles themselves; (iii) the rules on special meetings, which are regulated by article 2415, and not by article 2376 Italian Civil Code

Notwithstanding these specific rules, it makes no sense to state that such instruments cannot in any case be assigned administrative rights. It makes no sense because article 2346 permits the creation of "hybrid" instruments.

In other words, the articles could envisage the issue of participating financial instruments against a cash contribution, which carry administrative rights (with the broad freedom permitted by article 2346) and economic rights essentially equivalent to those specified in article 2411, paragraph 3 (i.e. with total or partial repayment upon expiry, commensurate with the performance of the corporation's business). What must be avoided in a case such as this is the risk that the law may be easily evaded; as a result, the quantitative limits envisaged by article 2412 on the issue of such instruments must in any case apply.

In reality, the problem should be approached from a different perspective: the issue is not so much whether a certain administrative right can be assigned to financial instruments similar to bonds, but rather whether the bond issue limits should be imposed on *hybrid* financial instruments, issued under article 2346, which envisage either total or partial repayment of the capital contributed, even where i) such instruments in some way *share the business risk*, with the measure of the repayment being linked to the corporation's financial results and ii) they carry *administrative* rights. The *hybridisation* of *quasi debt instruments* cannot exempt them from the provisions that limit their issue.

Instead, I can see no problem with regard to the body responsible for deciding their issue or the organisation that protects the rights of the holders of such *hybrid* instruments. Indeed, article 2411, paragraph 3, Italian Civil Code generally provides that the rules contained in

*Section* VII (on bonds) apply to all the financial instruments that we have defined "quasi debt instruments". However, this is *only* true for instruments without administrative rights, while for *hybrid* instruments (including participating instruments) there would clearly be problems of compatibility between the two sets of rules (as regards the body that may decide their issue – management board or articles/extraordinary shareholders' meeting – and as regards the holders' organisation – bondholders' organisation or participating instrument holders' organisation -). Indeed, in the case at hand, the "hybrid" financial instrument is part of the corporate organisation and (potentially) interferes with the shareholders' prerogatives. Moreover, the limited protection afforded to bondholders would make little sense in light of the powers of "self-protection" that the assignment of administrative rights provides for holders.

Thus, it must be concluded that the rules on bonds only apply *in their entirety* to *para-debt instruments* not carrying administrative rights, while such rules only apply in part (i.e. exclusively with regard to the quantitative limits on their issue) to instruments that carry administrative rights.

Although an intermediate solution – i.e. a case-by-case analysis of such *hybrid* instruments to ascertain the level of "contamination" by participating instruments – has been proposed in an intelligent manner by scholars[21], it is not wholly convincing. In effect, it would require the interpreter to verify whether the administrative rights assigned to the holder are sufficient to attribute an "organisational value within the corporation" to these financial instruments and only in this case would the rules on bonds be set aside. This interpretation is not acceptable because the parameter is too vague and uncertain.

In reality, it is a delicate issue of "establishing the boundaries", for which a clear solution would be preferable so as to prevent a race by financial engineers to create *hybrid* instruments, the logical conclusion of which would be that only the assignment of *minor* administrative rights would be compatible with the rules on debt instruments. What would such "minor" rights be?? The power to inspect the corporation's books[22]? Taking part but not voting in the shareholders' meeting (setting aside the often cited problem constituted by article 2370 Italian Civil Code, which means that it is now difficult to imagine a situation in which attendance and vote are separated)? "Atypical" generic powers of oversight/supervision? Moreover, the sole purpose of this effort would essentially be to ensure that it is the management board that issues the instruments. It would be much better to state categorically that if administrative rights are also assigned, the rules set forth in article 2346 and not those in articles 2411 *et seq*. will apply, subject to the quantitative limits envisaged by article 2412, which are – it must be repeated – applicable wherever there is a right to the repayment of the consideration, even if this is (in part) dependent upon the financial results.

Instead, financial instruments for participating in the transaction pose fewer regulatory problems: there are, in fact, fewer overlaps with the category of participating financial instruments in the case of *hybridisation* of the model envisaged by the Italian Civil Code. Here, as mentioned, the holder would, in principle, only have supervisory powers and not powers to "participate in the management". Therefore, additional rights – of supervision and information – could be assigned to him without resorting to instruments not envisaged by article 2447-*ter* Italian Civil Code

However, even in this case the *hybridisation* of the instrument would be possible, with the consequent application of the rules contained in article 2346 Italian Civil Code, including with regard to the special meeting, if one were to assign administrative rights that are not limited to management control. There would, however, be no mandatory provisions – as in the aforementioned case of the quantitative cap on the issue of bonds and similar instruments – except, perhaps, for article 2447-*sexies*, single paragraph, second sentence, which envisages an obligation to keep the book of financial instruments for participating in the transaction issued in a *nominative* form, which would be necessary in any case.

**9.** In conclusion, the holders of participating financial instruments may be assigned an extremely wide range of administrative rights. Despite the restrictions which must be recognised, sometimes even by "forcing" the new legislative provisions, the power to participate in the management of the corporation that may be assigned to third parties is considerable.

Nonetheless, although such third parties may be assigned greater administrative rights than those attributed to minority shareholders, they do not become parties to the corporate agreement[23].

In fact, participating instrument holders provide *consideration*[24], they do not make a contribution, and this gives rise to a different relationship to that of the corporate agreement. However, rather than a credit relationship – as in the case of corporate bonds – it would be preferable to define it as an associative relationship which may be equated to a partnership (*associazione in partecipazione*).

The consideration provided for financial instruments is in this case merely a *loan* to a business that continues to belong to *others*, regardless of which *administrative* powers are assigned to them. In essence, it would appear that, in this case, the legislator – which is not always clear in its choice of expressions – has purposely used the concept of "consideration" as a distinguishing feature.

This explains why the *substantive* limit on the issue participating financial instruments is that the issuer must not become an SPA *in the hands of non-shareholders*. However, since no quantitative criteria or strict, clear limits have been introduced (as they have in other legal systems), one can only evaluate the articles as a whole to check that an *abnormal* corporation, institutionally controlled by non-shareholders, has not been created.

[1] See Oppo, *Le grandi opzioni della riforma e la società per azioni*, in *Scritti giuridici*, VII, *Vario diritto*, Padova, 2005, p. 298.

[2] See Oppo, *Quesiti in tema di azioni e strumenti finanziari*, in *Scritti giuridici*, VIII, *Ultimi scritti*, Padova, 2013, p. 67.

[3] See in the US EASTERBROOK-FISCHEL, *Voting in Corporate Law*, in *The Journal of Law and Economics*, XXVI (1983), p. 399; in UK cfr. Davies, *Gower and Davies' Principles of Modern Company Law*, VII ed., London, 2003, p. 806; cfr. also Van Ryn, *Securities and Securities Holders*, in *Int. Enc. of Comp. Law*, XIII, 5, Tübingen, 1990, n. 181, 116.

[4] See Tombari, *Le categorie speciali di azioni nella società quotata*, in *Riv. soc.*, 2007, p. 972.

[5] See Tucci, *La costituzione e i quorum*, in Lener-Tucci, *L'assemblea delle società per azioni*, Torino, 2012, p. 142 ss.

[6] See Angelici, *La riforma delle società di capitali. Lezioni di diritto commerciale*, Padova, 2006, p. 71.

[7] See Pomelli, *Rischio di impresa e potere di voto nella società per azioni: principio di proporzionalità e categorie azionarie,* in *Giur. Comm*., 2008, I, p. 530 ss.

[8] See Notari, *Le categorie speciali di azioni,* in *Il nuovo diritto delle società. Liber amicorum Gian Franco Campobasso,* I, Torino, 2006, p. 603.

[9] The prohibition on leonine agreements is, however, "too little" to limit the inequalities between categories of shareholders.

[10] See Oppo, *Spunti problematici sulla riforma delle società per azioni*, in *Scritti giuridici*, VII, cit., p. 275.

[11] See Oppo, *Sull'impatto sistematico della riforma del diritto societario*, in *Scritti giuridici,* VII, cit. p. 303 s.

[12] See the considerations in Oppo, *Principi (di diritto commerciale)*, in *Scritti giuridici*, VII, cit., p. 163.

[13] See Oppo, *Patto sociale, patti collaterali e qualità di socio nella società per azioni riformata*, in *Scritti giuridici*, VII, cit., p. 322.

[14] See Lener, *L'intervento in assemblea*, in Lener-Tucci, *L'assemblea*, cit., p. 97 ss.

[15] See Desana, *Le categorie di azioni e gli strumenti finanziari non azionari*, in *La riforma delle società, profili della nuova disciplina*, Torino, 2003, p. 124 ss.

[16] Cfr. Cian, *Strumenti finanziari partecipativi e poteri di voice*, Milano, 2006, p. 107 ss.; in the US see Williamson, *Corporate Governance*, in *Yale Law Journal*, 93 (1984), p. 1206 ss.

[17] With the consequence that the management board will increasingly become a place of confrontation and discussion, including with the non-shareholders' representatives, and not just of management decisions.

[18] See Cian, *Strumenti finanziari partecipativi e poteri di voice*, cit., p. 105 ss.; Cossu, *Società aperte e interesse sociale*, Torino, 2006, p. 207 ss.; Lamandini, *Autonomia negoziale e vincoli di sistema nella emissione di strumenti finanziari da parte delle società per azioni e delle cooperative per azioni*, in *Banca, borsa*, 2003, I, p. 536. Cfr. also Pennington, *Company Law*, VIII ed., London, 2001, p. 648 s.; Davies, *Gower and Davies' Principles*, cit., p. 307; in Germany cfr. Schmidt, *Gesellschaftsrecht*, IV ed., Köln-Berlin, 2002, § 28, III, p. 832; for a different solution in Switzerland see § 709 OR.

[19] See Valzer, *Gli strumenti finanziari partecipativi e non partecipativi nelle società per azioni,* Torino, p. 306 ss.

[20] See Valzer, *op. cit.*, p. 353 ss.; Dentamaro, *Le obbligazioni*, in *Il nuovo diritto societario nella dottrina e nella giurisprudenza*, Bologna, 2009, p. 250 ss.; Giannelli, *sub Art. 2411*, in *Commentario*, directed by Marchetti, Bianchi, Ghezzi and Notari, Milano, 2006, p. 61 ss.

[21] See Cian, *Strumenti finanziari partecipativi*, cit.

[22] Under German Law see Hüffer, *Aktiengesetz*, VI ed., München, 2004, § 221, p. 1072; Lutter, in *Kölner Kommentar zum Aktiengesetz*, Bd 5/1, II ed., Köln-Berlin, 1995, § 221, Rn 220, 584.

[23] See Oppo, *Patto sociale*, cit., p. 324.

[24] On the different meaning of *apporto* (*consideration*) of the *contractual* view and of the *institutional* views of SPAs, see Oppo, *Le grandi opzioni*, cit., p. 287.

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# Open Review of Management, Banking and Finance

«They say things are happening at the border, but nobody knows which border» (Mark Strand)

# Recovery plans in the context of the BRRD framework

by **Vincenzo Troiano**

**Abstract:** the BRRD contributes to the establishment of the new EU regulatory framework on the measures to be adopted for the prevention and early intervention in the event of financial instability of credit institutions, which is a matter that stands at the crossroad between prudential supervision and resolution interventions. This article focuses on the analysis of substantive and procedural aspects relating to the drawing-up and approval of "recovery plans" in their role of *preparation instruments* established under BRRD as well as *governance arrangements* of banks under the meaning of the CRD 4. The analysis aims also at highlighting the distinction and similarities of "recovery plans" with the "resolution plans", i.e. the other main *preparation instrument* provided for in the BRRD. Only time and practice will allow a detailed assessment of the relevance and effectiveness of the preparatory and preventative instruments provided for by the BRRD. However, at the moment it is already clear that "recovery plans" will play a key role in the improvement of corporate governance arrangements and will foster the development of a new culture of risk management in banks and financial companies.



1. The area of *recovery plans* falls under the broader framework of prevention and early intervention in the event of situations of financial instability affecting credit institutions, which was subject to close attention in the wake of the 2008 financial crisis. This area, which serves as an interface, in light of its positioning within the system, between prudential supervision instruments and resolution instruments, is characterized by the latent ambiguities intrinsic in such framework: this applies with regard to both the link (that is established in this context) between competent and resolution authorities, as well as the identification of compatibility of injunctive measures which regulatory authorities may imposed during the plan assessment phase with principle of the freedom to conduct a business. I will first analyze recovery plans in

the context of the *preparation instruments* established under directive 2014/59/EU, known as the BRRD, delineating distinctions and continuity with respect to resolution plans, another preparation instrument governed by the same EC legal base. Then I will analyze recovery plans as *governance arrangements* of banks, and later analyze more closely the *substantive aspects* of the above-mentioned plans and *criteria for assessing and approving* such plans. As for the method followed in this article, reference will be made exclusively to the BRRD, since it is quite clear, in consideration of the authorities involved, that all of the rules deriving from the application of the Single Supervisory Mechanism (and therefore of the role of the ECB with respect to intermediaries exceeding the relevant threshold and eventually also those below the threshold) and the Single Resolution Mechanism (with regard to the structure of the resolution authority) will apply. On the other end, the matters subject to analysis will be addressed individually, given that the relevant legal framework sets forth distinct provisions applicable to group plans, without such circumstance giving rise to any substantive implications with respect to the analysis[1].

2. The directive, drawing from the experience of the financial crisis, aims at establishing a credible recovery and resolution framework for credit institutions, in order to prevent to the extent possible the need to intervene with rescues of credit institutions using taxpayer funds; it aims at preventing insolvency and, in the event of insolvency, to reduce its adverse impacts. The improvement of the capital adequacy and prudential instruments provided by CDR IV should reduce – in the hopes of European lawmakers – the likelihood of future crises; however, the risk that credit institutions may face difficulties cannot be considered eliminated. With this risk in mind, there was a need to endow authorities with a set of instruments that allow for interventions that are sufficiently early and rapid for intermediaries facing financial crises or instability[2]. The focus placed by the lawmakers upon the preparation and planning of interventions to be implemented in case of unfavorable circumstances is considerable. The early analysis of possible adverse scenarios and measures that may be taken if such adverse scenarios were to materialize, should serve as a safeguard to protect the functioning of the system as a whole (including various actors consisting of entities and competent and resolution authorities) to react quickly and early upon the emergence of situations of instability. While this, from a functional standpoint, constitutes the main feature of the "preparation phase", it should be noted that such phase will have to be structured differently depending upon whether it is aimed at preparing the recovery of the entity in difficult or the resolution of the crisis faced by the entity. The directive indeed identifies two separate measures comprising the preparation phase, revolving around recovery plans and resolution plans: the former contain measures aimed at restoring the financial situation of an entity after a significant deterioration of the same; the latter include resolution actions that the competent authority may implement when the entity meets the conditions for resolution provided under the directive.

The two instruments differ in several respects: the most important distinctions regard (i) the entities responsible for the drawing up of the plans; (ii) the authorities involved in the drawing up and approval process; (iii) more generally, the systematic role of the two instruments.

*On the drawing up.* Recovery plans are drawn up by credit institutions (it is true that the directive envisages dialogue during the plan preparation and assessment phase, but the plan remains an instrument that is drawn up and approved by the lending institution); on the contrary, the resolution plans are drawn up by the competent resolution authority, the entity subjected to the plan does not play an active role (at least in principle), but rather is explicitly subjected to significant obligations to report to and cooperate with the authority in charge of preparing the resolution plan. This differences in structure with regard to the responsibility for drawing up the plans shows that, in the event of recovery, precedence was given to the autonomy of the concerned enterprise in assessing, in a forward-looking manner, the appropriate responses to deterioration in its financial condition; on the other hand, in the case of resolution, precedence is given to the public interest underlying the orderly management of crises, also considering the possible systemic impact of the same.

*As for the authorities* that take part in the plan adoption phase, the competent authorities of the individual entities that have prepared the recovery plan are the ones to carry out the assessment on the adequacy of the plan (in this regard, the role of the resolution authorities is limited to the possibility of formulating recommendations to the competent authority with regard to those actions envisaged under the plan that could have an adverse impact during a possible resolution phase); the resolution plan is – on the other hand – directly implemented by the entity's resolution authority (and, in this case, the competent authority's position is limited to cooperation with the resolution authority in gathering information necessary for the preparation of the plan).

It is clear from the foregoing considerations, with regard to the *systematic role* of the two instruments being compared, that recovery plans fall more clearly under the supervisory area, whereas resolution plans fall within the area of crisis management or resolution.

The recovery plans are positioned intrinsically within the ambit of *ex-ante* tools, as instruments through which a default may be prevented by imposing measures to be implemented in order to stabilize the financial situation of a bank; resolution plans are positioned conceptually within the ambit of *ex-post* tools, as corrective measures to be taken if a default becomes inevitable.

That said, it is worth noting that recovery plans, if they pertain to an entity that is not facing financial difficulties, nonetheless plan the measures to be implemented in order to overcome a hypothetical situation of deterioration; conceptually, they fall on the border between the areas of prudential supervision and crisis management. All of the foregoing occurs within and overarching context that does mark a clear line between the two areas and, in fact, tends to bring forward the assessments typical of a crisis situation to a much earlier moment, while from a different perspective, it creates authorities that have to remain separate, if not from a subjective standpoint, at least from a functional standpoint. The institutional and functional structure introduced by the directive (as supplemented by the Single Supervisory and Single Resolution mechanisms) must lead to the consolidation over time of roles and responsibilities, which to date has not been thoroughly defined.

A last remark, with regard to the system, concerns the significant role assigned to the EBA in this area. If we focus our attention solely on recovery plans, the EBA is called upon to prepare *draft regulatory technical standards*, for example, to define the criteria for the assessment of the systemic impact of the failure of an institution (which is relevant for purposes of eventually simplifying the obligations to prepare the plan), to specify the information to be included in the plans, to define the criteria for assessment of plans prepared by banks. It is also called upon to issue *guidelines* in order to define the range of stress scenarios to be considered in the preparation of plans. It results a varied and robust set of responsibilities aimed at achieving the objective of ensuring a uniform structure comprising the various authorities in charge of applying the new legal framework.

3. The directive indicates that recovery plans are to be considered a governance *arrangement* under art. 74 of CDR IV (directive 2013/36/EU). The provision of CRD IV just cited already envisaged the fact that the competent authorities ensured the drawing up by banks of recovery plans aimed at restoring their financial situation following a significant deterioration. The BRRD, moreover, expressly qualifies the plans in question as governance arrangements and, therefore, from a standpoint of prudential oversight, the drawing up of such plans, their implementation, monitoring periodic updating and so forth fall squarely under the legal framework of the CDR IV with regard to governance arrangements[3].

As known, governance arrangements consist of all those mechanisms, procedures, processes, technical means, organization of such factors, remuneration policies, aimed at collectively achieving and ensuring the governance and internal functioning of a bank. All of this is accomplished through an overarching structure that ensures the effective and prudent management of the bank and, in particular, the risks to which it is exposed. Considered from this perspective, namely as a governance arrangement, the recovery plan (*rectius*, its adoption) becomes a key instrument through which one of the main functions assigned by the EU to management body of credit institutions is exercised. The management body is assigned with general responsibility over the bank, approving and overseeing, *inter alia*, the implementation of its risk strategy (this has already led to the management body's exposure to the adoption of banks' Risk Appetite Framework). Within this context, the approval of the recovery plan, especially in consideration of the contents that such plan will have to have, constitutes an exercise in which the management body will have to demonstrate thorough awareness of the bank's position and all of the circumstances that may jeopardize its stability. In performing such exercise, the management body may also decide to adopt measures immediately, aimed at reducing the identified sources of exposure to potential risk and underlying the scenarios envisaged under the plan. Construed in these terms, the approval and update of recovery plans may constitute an element of discipline in the performance of the duties of the management body regarding the bank's policies on the control of the exposure to risks[4].

On another front, the particular depth of the analysis required during the assessment of recovery plans confirms the need, that has for some time been noted in the legal framework applicable to the sector, to enhance the qualitative composition of boards of directors: in this sense, the depth of knowledge and diversified areas of specialized expertise constitute, for the management body as a whole, a fundamental requisite in order to be in a position to effectively fulfill the management body's duties of examining and approving the plans in question.

4. The directive sets forth, in an Annex thereof, the information to be included in the recovery plans. Such information constitute the minimum set of indications for the preparation of plans by entities of systemic importance (*rectius*: for entities subject to direct supervision on the part of the ECB or those that represent a significant part of the financial system of their home member state).

The national authorities may supplement this minimum set of information, and may also proceed, with regard to entities other than those of systemic important, to simplify the information to be included in plans and the timetables for updates and revisions to the same.

This is a particularly broad power which is dependent upon the satisfaction of a number of general criteria set by the directive: this is in order to ensure that the obligation to prepare recovery plans is applied *appropriately and proportionately*, minimizing the administrative costs related to the preparation of such plans[5].

In reality, the criteria identified by the directive are extremely broad in scope. In order to allow the simplification, competent authorities must assess the potential impact that the failure of the concerned entity could have on the financial markets, other entities and lending conditions as well as the economy in general. Such assessment, in turn, should be conducted taking into account, *inter alia*, the type of business pursued by the entity and the complexity of the same (including the performance or not of investment services), its shareholding structure, legal form, risk profile, size, legal status and interconnections between the entity and other entities or with the financial system in general, whether or not it belongs to an institutional protection system or other systems of mutual solidarity for cooperative credit institutions.

From a standpoint of contents, in addition to the disclosure set forth in the Annex to the directive, recovery plans (i) *must not* assume access to or receipt of extraordinary public financial support, (ii) *must include* any measures that the entity may adopt in the event that conditions are met for an early intervention within the meaning set forth in article 27 (and, in other words, the breach or risk of breach of one of the requisites established under the "CDR IV package": directive 2013/36/EU and EU regulation no. 575/2013); (iii) *must indicate* the procedures to ensure the timeliness of the recovery actions planned.

In addition, recovery plans must indicate the measures that entities will be required to take to restore their financial situation following significant deterioration; they must be detailed and *based upon realistic scenarios*, applicable in a series of (valid and rigorous) situations of serious macroeconomic and financial stress pertaining to the specific situation of the entity (and including event of a systemic nature and specific stress event for individual legal entities and groups)[6], and include the set of *indicators*, of a qualitative or quantitative nature, established by the entity and the circumstances in which the actions indicated in the plan may be implemented[7].

The breadth of simplification powers and the importance of detailed data needed in the definition of the required indicators and stress scenarios may theoretically lead to an effective risk of substantial fragmentation in the regime applicable to entities in different jurisdictions; this justifies the assignment to the EBA of the power to issue guidelines or draft regulatory technical standards, related to various aspects pertaining to the drawing up of the plans: this applies, for example, as regards the criteria to be used to assess the impact of the failure of one entity on the financial market, other entities, and lending conditions; or with regard to the scenarios to be used and the list of quantitative and qualitative indicators[8].

In cases in which the instrument to the used by the EBA consists of guidelines, the lack of binding value which is inherent in such instrument opens the door to the risk of an incomplete harmonization as regards the drawing up of the plans.

5. The recovery plan prepared by the competent bodies of bank, based upon its ordinary governance mechanisms, is subject to review and approval by the bank's management body, before being submitted to the competent authority[9]. The recurring reference to the fact that the management body must *examine* the draft plan for approval is an indication of the need of its full involvement in analyzing the contents of the plan.

The management body's review is not merely procedural (i.e. for compliance with the internal process for the preparation of the plan), or aimed at assessing its completeness (i.e., to verify that the plan effectively contains the required information, the scenarios envisaged under the directive, the indicators, that will later be agreed at the time of its assessment), but rather also focuses on the matter of the various choices set forth in the document, with regard to both the establishment of the scenarios and the qualitative and quantitative indicators, and the measures that are planned to be activated upon the occurrence of the circumstances envisaged under the plan. From this latter standpoint, the measures may include instruments or initiatives (albeit merely planned) that also affect the bank's strategic decisions, which must necessarily be submitted to the board of directors for approval. In these terms, the configuration of the recovery plan as a governance arrangement of the entity is plain to see.

Once approved, the plan is subjected to a "complete assessment" by the competent authority which has to verify its thoroughness and capacity to restore the solvency of the entity in a timely manner, including during periods of serious financial stress[10].

In particular, the assessment performed by the authority is aimed, on the one hand, at verifying that the contents of the plan meet the content-related requisites established by the directive; on the other, it is aimed at certifying the *reasonable likelihood* that the implementation of the provisions proposed in the plan preserves or restores the economic sustainability and the financial condition of the entity (taking into account the preparatory measures that the entity has taken or intends to take), and that the operating options contained therein work quickly and effectively in situations of financial stress (avoiding to the extent possible material adverse effects on the financial system, including in scenarios that would lead other entities to implement recovery plans in the same period).

In making such assessment, the competent authority has to take into consideration the capital adequacy and the funding structure of the entity compared to the level of complexity of the organizational structure and the risk profile of the same entity.

The assessment phase is an interactive process: if the authority finds that the plan presents *material* deficiencies or that its implementation is subject to *material* impediments, it formally notifies such assessment and asks the entity to present (within two months) an amended plan that indicates how it is remedying such deficiencies or impediments. If the amended plan is also found to be inadequate to remedy the deficiencies and impediments, the competent authority may direct the entity to make specific amendments, setting a deadline for remedying the deficiencies or impediments to the plan's implementation.

In the absence of the foregoing, the competent authority may force the entity to take the measures considered necessary and proportionate, taking into account the seriousness of the deficiencies and impediments and the effect of the measures on the entity's business operations. Taking into account the principle of proportionality, the measures in question may, *inter alia*, concern a reduction in the entity's risk profile; the activation of recapitalization measures; the re-examination of the entity's strategy and structure; and the modification of the governance structure.

The inclusion of an obligation for an entity to modify its plan with interventions that may concern the structure or governance of the entity may have a general impact upon the freedom to conduct a business guaranteed by article 16 of the EU Charter of Fundamental Rights[11]; it should be recalled in this regard that at the time of drafting the recovery plan, the entity in question is not in a state of financial deterioration, but is rather preparing and planning actions and remedies for the possibility that certain adverse events may occur, which are credible but not necessarily probable. The directive, indicates that such limitation would be in line with the provisions of art. 52 of such Charter: this is due to the fact that the limitation in question would be *necessary* (in order to meet the objectives of financial stability and, in particular, to reinforce the entities' business operations and prevent them from growing too quickly or assuming excessing risks without being in a position to address difficulties and losses and to restore a capital base) and *proportionate* (because it allows for preventative action of a nature and scope necessary to remedy the deficiencies) [12].

Obviously, such compatibility pertains to the introduction of provisions to the EU legal framework that enables the competent authorities to take measures of such type. The same criteria of *strict necessity* and *proportionality* must necessarily constitute the criteria for checking the lawfulness of the exercise by public authorities of the power to impose injunctions (as provided for in the directive), that in light of the compliance of such powers with the freedom to conduct a business guaranteed under art. 16 of the EU Charter of Fundamental Rights.

As for responsibility, it is fair to consider that the approval of supplementary and replacement measures required by the authority also rests with the management body, like the adoption of the plan.

One last remark has to be made on the role of the management body on this matter, drawing from the legal framework set forth in article 9 of the directive, related to the activation of the measures envisaged under the plan, upon the occurrence of circumstances covered by the qualitative and quantitative indicators included in the plan. In such regard, the directive expressly provides that the entity may take action in the context of its recovery plan also when the pertinent indicator has not been satisfied if the entity's management body deems it advisable under the circumstances or, alternatively, may refrain from taking action when the entity's management body does not consider such action advisable under the circumstances.

In the cases the management body's decision is doubtlessly highly important, since it is in practice deviating from what provided in the plan. It goes without saying that a decision by the management body not to implement what provided in the plan, resulting in a worsening of the entity's financial situation (eventually triggering even the adoption of early intervention measures), may end up exposing the management body to potential claims and criticisms from various sources (in addition to the authority, which could initiate supervisory actions even in the event of a decision not to proceed in accordance with the plan, shareholders and creditors may also have an interest in raising claims).

6. Concluding remarks regarding a legal framework that is still at such a preliminary stage must necessarily be limited to pointing out that only time and practice will enable an assessment of the relevance and effectiveness of the preparatory and preventative instruments in question; nonetheless it can certainly be concluded from the very outset that these are instruments that are destined to play a key role in the improvement of corporate governance arrangements and mechanisms for fostering a culture of risk awareness and control at the level of banking and financial companies.

[1] See Recital (11) BRRD, according to which *"In order to ensure consistency with existing Union legislation in the area of financial services as well as the greatest possible level of financial stability across the spectrum of institutions, the resolution regime should apply to institutions subject to the prudential requirements laid down in Regulation (EU) No 575/2013 of the European Parliament and of the Council and Directive 2013/36/EU of the European Parliament and of the Council. The regime should also apply to financial holding companies, mixed financial holding companies provided for in Directive 2002/87/EC of the European Parliament and of the Council (3), mixed-activity holding companies and financial institutions, when the latter are subsidiaries of an institution or of a financial holding company, a mixed financial holding company or a mixed-activity holding company and are covered by the supervision of the parent undertaking on a consolidated basis. The crisis has demonstrated that the insolvency of an entity affiliated to a group can rapidly impact the solvency of the whole group and, thus, even have its own systemic implications. Authorities should therefore possess effective means of action with respect to those entities in order to prevent contagion and produce a consistent resolution scheme for the group as a whole, as the insolvency of an entity affiliated to a group could rapidly impact the solvency of the whole group."* See, *inter alia*, Babis, *European Bank Recovery and Resolution Directive: Recovery Proceedings for Cross Border Banking Groups, University of Cambridge, Faculty of Law Research,* Paper no. 49, 2013, p. 4 et seq.

[2] More in general, see Recital (5) BRRD: "*a regime is therefore needed to provide authorities with a credible set of tools to intervene sufficiently early and quickly in an unsound or failing institution so as to ensure the continuity of the institution's critical financial and economic functions, while minimising the impact of an institution's failure on the economy and financial system. The regime should ensure that shareholders bear losses first and that creditors bear losses after shareholders, provided that no creditor incurs greater losses than it would have incurred if the institution had been wound up under normal insolvency proceedings in accordance with the no creditor worse off principle as specified in this Directive. New powers should enable authorities, for example, to maintain uninterrupted access to deposits and payment transactions, sell viable portions of the institution where appropriate, and apportion losses in a manner that is fair and predictable. Those objectives should help avoid destabilising financial markets and minimise the costs for taxpayers*".

[3] See Art. 5 BRRD.

[4] See, *inter alia*, Amorello – Huber, *Recovery planning: a new valuable corporate governance framework for credit institutions*, in *Law and Economics Yearly Review*, 2014, p. 314; John – Litov – Yeung, *Corporate Governance and Risk Taking*, in *The Journal of Finance*, Vol. 63, Issue 4, 2008, p. 1679 – 1728 et seq.; Laeven – Levine, *Bank Governance, Regulation, and Risk Taking,* in NBER Working Paper No. 14113, 2008; Stulz, *Governance, Risk Management, and Risk-Taking in Banks*, in ECGI Finance Working Paper No. 427/2014, 2014.

[5] In particular, according to Recital (14) BRRD: *"Authorities should take into account the nature of an institution's business, shareholding structure, legal form, risk profile, size, legal status and interconnectedness to other institutions or to the financial system in general, the scope and complexity of its activities, whether it is a member of an institutional protection scheme or other cooperative mutual solidarity systems, whether it exercises any investment services or activities and whether its failure and subsequent winding up under normal insolvency proceedings would be likely to have a significant negative effect on financial markets, on other institutions, on funding conditions, or on the wider economy in the context of recovery and resolution plans and when using the different powers and tools at their disposal, making sure that the regime is applied in an appropriate and proportionate way and that the administrative burden relating to the recovery and resolution plan preparation obligations is*

*minimised. Whereas the contents and information specified in this Directive and in Annexes A, B and C establish a minimum standard for institutions with evident systemic relevance, authorities are permitted to apply different or significantly reduced recovery and resolution planning and information requirements on an institution-specific basis, and at a lower frequency for updates than one year. For a small institution of little interconnectedness and complexity, a recovery plan could be reduced to some basic information on its structure, triggers for recovery actions and recovery options. If an institution could be permitted to go insolvent, then the resolution plan could be reduced. Further, the regime should be applied so that the stability of financial markets is not jeopardised. In particular, in situations characterised by broader problems or even doubts about the resilience of many institutions, it is essential that authorities consider the risk of contagion from the actions taken in relation to any individual institution."*

[6] See Art. 7 – 8 BRRD.

[7] See Art. 9 BRDD.

[8] In particular, see the final report by EBA on *"Guidelines on the minimum list of qualitative and quantitative recovery plan indicators"* (6 May 2015), identifying the minimum qualitative and quantitative indicators that institutions should include in their recovery plans.

[9] See art. 6 et seq. BRRD.

[10] In particular, according to Recital (21) BRRD: *"it is essential that institutions prepare and regularly update recovery plans that set out measures to be taken by those institutions for the restoration of their financial position following a significant deterioration. Such plans should be detailed and based on realistic assumptions applicable in a range of robust and severe scenarios. The requirement to prepare a recovery plan should, however, be applied proportionately, reflecting the systemic importance of the institution or the group and its interconnectedness, including through mutual guarantee schemes. Accordingly, the required content should take into account the nature of the institution's sources of funding, including mutually guaranteed funding or liabilities, and the degree to which group support would be credibly available. Institutions should be required to submit their plans to competent authorities for a complete assessment, including whether the plans are comprehensive and could feasibly restore an institution's viability, in a timely manner, even in periods of severe financial stress"*.

[11] See Art. 16 of the Charter of fundamental rights of the European Union: *"Freedom to conduct a business in accordance with Union law and national laws and practices is recognised"*.

[12] See Recital (24) BRRD.

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